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S. HRG. 100-952

TELEMARKETING FRAUD

HEARING

BEFORE THE

SUBCOMMITTEE ON THE CONSUMER

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION
UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

SECOND SESSION

ON

S. 2213 and H.R. 4101

TO AMEND THE FEDERAL TRADE COMMISSION ACT TO STRENGTHEN THE AUTHORITY OF THE FEDERAL TRADE COMMISSION RESPECTING FRAUD COMMITTED IN CONNECTION WITH SALES MADE WITH A TELEPHONE

S. 2326

TO ENHANCE THE FEDERAL TRADE COMMISSION'S ABILITY TO PREVENT CONSUMER FRAUD

SEPTEMBER 13, 1988

Printed for the use of the
Committee on Commerce, Science, and Transportation

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TELEMARKETING FRAUD

TUESDAY, SEPTEMBER 13, 1988

U.S. Senate,
Subcommittee on the Consumer,
Committee on Commerce, Science, and Transportation,
Washington, D.C.

The subcommittee met at 2:30 p.m. in room SR-485, Russell Senate Office Building, Hon. Albert Gore, Jr., [chairman of the subcommittee] presiding.

Staff members assigned to this hearing: Kevin Curtin and Linda Lance, staff counsels; and Chuck Harwood, minority staff counsel.

OPENING STATEMENT BY SENATOR GORE

Senator Gore. The subcommittee will come to order. The first order of business is an apology from the subcommittee to our witnesses, particularly those on our first panel, and to all of our guests.

Both sides of the aisle were advised that we would have a vote right at 2:00 o'clock and Senator McCain and I were attempting to avoid discourtesy by voting right at 2:00 and rushing over there to vote. They put it off until 2:10 and, as you can see from the bell, we just had the vote. So we were trying to be courteous and not discourteous, but we got fouled up by a change in plans in the order of business over on the floor.

Well, enough of that. Let us not compound it. Let me rush through my opening statement by saying that we are going to consider telemarketing fraud legislation today that I and others have introduced and that passed the House of Representatives earlier this year, as well as consumer fraud legislation introduced by the ranking Republican member of our subcommittee, Senator McCain.

I introduced legislation in the Senate because it seems apparent to me that we must provide additional protection for consumers who purchase goods and services over the telephone. This protection is important because telephone sales are becoming more and more popular.

Industry sources estimate that there were almost $120 billion in sales made over the telephone in 1986 and more than that last year, although the figures are not yet complete.

Catalogue sales and legitimate purchases are being made in greater and greater numbers. Today a consumer can purchase almost any item over the phone and charge the purchase to their credit card account.

Well, when you have a convenient and profitable arrangement, I guess it is only a matter of time before some unscrupulous individuals find a way to take advantage of it. Con artists have discovered the fertile telemarketing marketplace.

Some have suggested that telemarketing fraud ought to go by the slogan "Reach out and cheat someone,' for that is exactly what is now happening. There is no mistaking it, telemarketing fraud is a billion dollar a year illicit industry that most often involves the offer of goods and services at discount purchases or offers that are simply too good to be true.

Payment is generally required in advance and then, if the product arrives, the consumer finds that the bargain does not exist or is not of the promised value. Sometimes, of course, the item never even reaches the consumer.

What kinds of products are fraudulently offered for sale? Well, we have found that these schemes have involved the sale of vitamins, diet aids, credit card protection programs, luggage, vacation arrangements, office machine supplies, and a whole host of other consumer commodities.

Let me review a few brief examples. Three nationwide telemarketers deceived consumers by selling them so-called vacation passports. Under this plan, consumers paid between $289 and $350 for a passport which supposedly entitled them to fully paid vacations to Hawaii and other places, including round trip air fare and hotel lodging for eight days and seven nights.

The only extra cost was to be an economy air fare. Credit card numbers were requested, of course, solely to verify the consumer's eligibility to buy the passport. In reality, substantial additional sums were required. The air fare was the most expensive available coach air fare and costs were billed to the credit cards without authorization.

Fortunately, these particular perpetrators were caught and brought to justice. But many others go scot-free.

In another case, telemarketers fraudulently promised to match consumers with overseas jobs that were never delivered. Tens of thousands of consumers were bilked out of millions of dollars.

In Georgia, the owner of a day care center reportedly purchased $4,000 worth of pens imprinted with her business logo in return for vouchers for vacation trips which she planned to give to her employees. When she called to cash in the vouchers, the company's phone had been disconnected.

Just within the past week, we have heard incredible reports that telephone con artists sold piles of dirt that supposedly contained gold to the tune of $250 million per year. However, all the consumers really ended up receiving was a pile of dirt. It contained microscopic amounts of gold, less than that contained in sea water.

Well, the ingenuity of these con artists is evidently limitless. If a consumer is not attracted by dirt piles with gold in them, he or she can buy fake rare coins, overpriced diamonds, and imitation Salvador Dali paintings.

It is not just gullible people who are being swindled. Press reports claim the victims include a lieutenant governor and a Federal judge. The fraud involves a cross-section of Americans, including small business, the elderly, and middle income persons.

This has become a nationwide problem. Legitimate businesses that engage in telemarketing are hurt by this fraudulent behavior and want to see it brought to an end because consumers become more afraid to purchase goods by telephone.

Consumers and honest businesses alike are suffering, and something must be done to turn the tide.

We are going to receive testimony from various parties involved in these issues this afternoon, including the Federal Trade Commission, the state attorneys general, representatives of industries involved in telemarketing, consumers, and a health care provider.

Our first witness will be Congressman Tom Luken. But before going to Congressman Luken, I want to recognize at this point Senator McCain, the ranking Republican member of the subcommittee, for his comments.

OPENING STATEMENT BY SENATOR McCAIN

Senator McCAIN. Thank you, Mr. Chairman. I would also like to thank you for calling the hearing today on this very important subject which we both find very troubling, as do millions of Americans.

As you mentioned, Mr. Chairman, consumer fraud costs the American taxpayers tens of billions of dollars a year, and it has also cost lives as well. And those who perpetrate acts of fraud against the American consumer do not discriminate. They prey on people of both sexes, of all ages, and at all levels of income.

Consumer fraud takes many forms, from telemarketing fraud to health quackery, and from fraud in the life care industry to deceptive mailings sent to seniors regarding their social security benefits.

It is wrong, and it is a very serious problem. I know the distinguished chairman, as have I, has had a long-running concern about this issue. In fact, we have each introduced legislation in this session addressing the problem of consumer fraud.

While they differ as to approach, both bills reflect the belief that current law should be improved to swiftly and effectively deal with telemarketing fraud.

In addition, my bill goes beyond telemarketing to cover other areas of consumer fraud, such as health care quackery and fraud in the life care industry.

I represent a state which has a considerable number of older Americans. While consumer fraud certainly affects people of all ages, I have come to find that seniors are particularly susceptible and targeted for fraudulent practices.

This is evidenced by a recent House Aging Committee finding that older Americans are being taken for over $10 billion a year as a result of health care quackery.

An advertisement was recently placed in the Arizona Republic and Phoenix Gazette newspapers that read: "Alzheimer's Disease, symptoms of senility; at last now there is hope. Call' a certain number "for help. Free, no charges, no fees." Obviously, that organization knew something that we do not. Well, the fact is that this fraud ripped off the citizens of my state to the tune of tens of thousands of dollars.

As a result of my exposure to the magnitude of fraudulent practices committed against older Americans, I have authored a bill targeting both telemarket fraud and other practices. It is my hope, Mr. Chairman, that as this subcommittee addresses how to appropriately beef up enforcement authority so that agencies will be able to more effectively deal with perpetrators of consumer fraud, that we would take a comprehensive approach to the issue of consumer fraud.

I look forward to hearing the testimony of this afternoon's witnesses and have high hopes for the things we might learn as to the scope of the problem, as well as the witnesses' opinions about what is necessary to strengthen the fight against consumer fraud.

And again, Mr. Chairman, I look forward to working with you to report legislation out of this subcommittee that both of us can strongly support and that will bolster the fight against consumer fraud, a fight that would hopefully result in more perpetrators of consumer fraud being put out of business, the business of ripping off the American consumer.

Thank you, Mr. Chairman.

Senator GORE. I certainly look forward to making it a bipartisan fight and reporting out legislation that has a realistic chance of passing this year.

[The bills follow:]

100TH CONGRESS
2D SESSION

S. 2213

To amend the Federal Trade Commission Act to strengthen the authority of the Federal Trade Commission respecting fraud committed in connection with sales made with a telephone.

IN THE SENATE OF THE UNITED STATES

MARCH 24 (legislative day, MARCH 21), 1988

Mr. BYRD (for Mr. GORE) introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

---

A BILL

To amend the Federal Trade Commission Act to strengthen the authority of the Federal Trade Commission respecting fraud committed in connection with sales made with a telephone.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE: REFERENCE.

(a) SHORT TITLE.—This Act may be cited as the "Telemarketing Fraud Prevention Act of 1988".

(b) REFERENCE.—Except as otherwise specifically provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Federal Trade Commission Act.

SEC. 2. COMMISSION AUTHORITY UNDER SECTION 19.

(a) STATE ENFORCEMENT.—Section 19 is amended by redesignating subsection (e) as subsection (l) and by inserting after subsection (d) the following:

"(e)(1) Any attorney general of a State and any other official of a State vested under State law with the authority to enforce State consumer protection laws may bring a civil action in the name of the State in a district court of the United States having jurisdiction of the defendant to secure relief, as provided in subsection (b), against any person, partnership, or corporation which engages in telemarketing which is a fraudulent or dishonest act or practice or which violates the rule promulgated pursuant to subsection (g) if the attorney general or other official alleges that such telemarketing affects or may affect the State or its residents.

"(2) No action may be commenced under paragraph (1) unless the Commission has been given written notice of the commencing of the action—

"(A) at least thirty days before the action is to be commenced, or

"(B) as early as practicable if the attorney general or other official commencing the action—

"(i) alleges that the harm to the public is ongoing, may recur, or presents an imminent hazard, and

"(ii) petitions the court for temporary or preliminary relief from such harm.

The Commission may intervene, by its own attorneys, in any such action, and the attorney general or other official of another State may intervene in any such action if the State or its residents are or may be affected by the telemarketing with respect to which the action is brought.

"(3) In an action brought under paragraph (1) a court may grant relief in the same manner and circumstances as it could if the action is brought by the Commission under subsection (a). Such relief may include relief relating to persons, partnerships, or corporations outside the State and relief applicable to conduct outside the State of any attorney general or other official who is a party to the action. An attorney general or other official of any State may petition any court which has jurisdiction of a person, partnership, or corporation subject to an order of a court granting relief to enforce such order with respect to such person, partnership, or corporation if the attorney general or other official alleges that failure to comply with such order affects or may affect such State or its residents.

"(4) For purposes of this section—

"(A) the term 'attorney general' means the chief legal officer of a State, and

"(B) the term 'State' includes the District of Columbia.".

(b) CITIZENS' SUITS.—Section 19, as amended by subsection (a), is amended by inserting after subsection (e) the following:

"(f)(1) Any person, partnership, or corporation may commence a civil action to secure relief, as provided in subsection (b), against a person, partnership, or corporation which engages in telemarketing which is a fraudulent or dishonest act or practice or which violates the rule promulgated pursuant to subsection (g). Such an action may be brought in a district court of the United States having jurisdiction of the defendant.

"(2) No action may be commenced under paragraph (1) unless the Commission has been given written notice of the commencing of the action at least thirty days before the action is to be commenced.

"(3)(A) In any action under paragraph (1), the Commission, if not a party, may intervene as a matter of right.

"(B) The court, in issuing any final order in any action brought under paragraph (1), may award costs of suit and reasonable fees for attorneys and expert witnesses if the plaintiff prevails.

"(C) Nothing in this subsection shall restrict any right which any person, partnership, or corporation may have under any statute or common law to seek enforcement of this Act or any rule or order under this Act or to seek any other relief.".

(c) REQUIREMENTS FOR TELEMARKETING.—

(1) Section 19, as amended by subsection (b), is amended by inserting after subsection (f) the following:

"(g)(1) The Commission shall promulgate rules for the telemarketing activities of a person, partnership, or corporation which engages in telemarketing. Such rules shall include a requirement that any person, partnership, or corporation engaged in telemarketing shall inform the person, partnership, or corporation to whom the telemarketing is directed that—

"(A) such person, partnership, or corporation is entitled to a refund of any money paid for the product or service which is the subject of the telemarketing if delivery of the product or service is not made—

"(i) within the time period included in the offer of the product or service, or

"(ii) if no time period is included in the offer, within thirty days of the date the offer is made, and

"(B) if such person, partnership, or corporation—

"(i) makes an unsolicited telephone call to a person, partnership, or corporation or otherwise communicates with such person, partnership, or corporation offering a free gift or prize or the substantial equivalent thereof and invites such person, partnership, or corporation to respond, and

"(ii) there is no Federal statute governing such solicitation involving the specific product or service offered or sold in connection with such solicitation,

such person, partnership, or corporation may cancel an order of such product or service not later than the expiration of three days after the date on which there is a sales agreement.

The rules shall include a rebuttable presumption that if a person, partnership, or corporation subject to the requirements of this paragraph does not keep adequate records to show compliance with such requirements such person, partnership, or corporation shall be considered to be in violation of such requirements.

"(2) Any person, partnership, or corporation who violates any rule promulgated under paragraph (1) shall be considered to have engaged in an unfair or deceptive act or practice in or affecting commerce.

"(3) The Commission shall promulgate the rules under paragraph (1) in accordance with section 553 of title 5 of the United States Code.".

(2) The Federal Trade Commission shall promulgate the rules prescribed by section 19(g) of the Federal Trade Commission Act (as added by paragraph (1)) within one hundred and eighty days of the date of the enactment of this Act.

(d) HARASSMENT.—Section 19, as amended by subsection (c), is amended by inserting after subsection (g) the following:

"(h) A person, partnership, or corporation which engages in telemarketing may not engage in any conduct the natural consequence of which is to harass, oppress, or abuse any person in connection with the telemarketing. A person, partnership, or corporation who engages in such conduct shall be considered to have engaged in an unfair or deceptive act or practice in or affecting commerce.".

(e) MULTIPLE DEFENDANTS.—Section 19, as amended by subsection (d), is amended by inserting after subsection (h) the following:

"(i) In an action brought under subsection (a), (e), or (f), a court may, whenever it appears to the court that the ends of justice require that other persons, partnerships, or corporations should be parties in such action, cause such parties to be summoned whether or not they reside in the district in which the actions were brought.".

(f) LIMITATION.—Section 19, as amended by subsection (e), is amended by inserting after subsection (i) the following:

"(j) For purposes of this section, a financial institution or other participant in a payment system used to pay for products or services offered or sold through telemarketing, including the credit or payment authorization aspect of such payment system, is not, by virtue of such participation, a person, partnership, or corporation which engages in telemarketing or acts in concert with, or on behalf of, a person, partnership, or corporation which engages in telemarketing.".

(g) DEFINITION.—Section 19, as amended by subsection (f), is amended by inserting after subsection (j) the following:

"(k) For purposes of this section, the term 'telemarketing' means the use of a telephone in the ordinary course of business to communicate with a person an offer for sale or to complete a sale of a product or service.".

SEC. 3. CLEARINGHOUSE.

The Federal Trade Commission shall establish a clearinghouse for inquires made to Federal agencies concerning telemarketing (as defined in section 19(k) of the Federal Trade Commission Act). The clearinghouse will provide information to persons making inquiries respecting persons, partnerships, or corporations engaged in telemarketing or direct such inquiries to the appropriate Federal or State agency.

○

II

100TH CONGRESS
2D SESSION

S. 2326

To enhance the Federal Trade Commission's ability to prevent consumer fraud.

IN THE SENATE OF THE UNITED STATES

APRIL 26 (legislative day, APRIL 25), 1988

Mr. MCCAIN introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

---

A BILL

To enhance the Federal Trade Commission's ability to prevent consumer fraud.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Consumer Fraud Prevention Act".

FINDINGS

SEC. 2. The Congress finds that—

(1) consumer fraud is a pervasive and persistent problem for American businesses and consumers;

(2) consumer fraud costs Americans billions of dollars each year, and it undermines legitimate commercial activities by businesses of all sizes and in all fields;

(3) consumer fraud schemes commonly exceed the jurisdictional boundaries of any single court or State;

(4) the perpetrators of consumer fraud use various means to escape prosecution, including rapid flight, jurisdictional diversity, and fictitious legal entities;

(5) one of the most pervasive types of consumer fraud is health fraud, which has been estimated to cost Americans more than $10,000,000,000 annually. In addition to being costly, such fraud can be life-threatening;

(6) consumer fraud involving telemarketing is estimated to cost consumers billions of dollars annually. Telemarketing involving investment fraud alone is estimated to cost $1,000,000,000 each year;

(7) the Federal Trade Commission and the attorneys general of the States have initiated a cooperative attack on telemarketing fraud. The success of this program has been hampered by jurisdictional limitations and inadequate resources;

(8) consumer fraud is a particular burden for senior citizens, who are more frequently defrauded than other consumers; and

(9) the ability of the Federal Trade Commission to attack consumer fraud has been limited due to inadequate authority, and legislation is needed to enhance

the Commission's ability to protect consumers from such abuses.

FALSE ADVERTISEMENTS CONCERNING SERVICES

SEC. 3. Section 12(a) of the Federal Trade Commission Act (15 U.S.C. 52(a)) is amended by inserting "services," immediately after "devices," each place it appears.

EXPANDED ENFORCEMENT TOOLS

SEC. 4. (a) VENUE.—(1) Subsections (a) and (b) of section 13 of the Federal Trade Commission Act (15 U.S.C. 53) are each amended by adding at the end thereof the following: "Whenever it appears to the court that the interests of justice require that any other person, partnership, or corporation should be a party in such suit, the court may cause such person, partnership, or corporation to be summoned whether or not they reside or transact business in the district in which the suit is brought, and to that end process may be served in any district.".

(2) Section 13 of the Federal Trade Commission Act (15 U.S.C. 53) is amended by redesignating subsection (c) as subsection (d) and inserting immediately after subsection (b) the following:

"(c) Any process of the Commission under this section may be served by anyone duly authorized by the Commission—

"(1) by delivering a copy of such process to the person to be served, to a member of the partnership to be served, or to the president, secretary, or other executive officer or a director of the corporation to be served;

"(2) by leaving a copy of such process at the residence or the principal office or place of business of such person, partnership, or corporation; or

"(3) by mailing a copy of such process by registered mail or certified mail addressed to such person, partnership, or corporation at his or her or its residence or principal office or place of business.

The verified return by the person so serving such process setting forth the manner of such service shall be proof of the same, and the return post office receipt for such process mailed by registered mail or certified mail as provided in this subsection shall be proof of the service of the same.".

(b) SUBPOENA.—(1) Section 20(a) of the Federal Trade Commission Act (15 U.S.C. 57b–1(a)) is amended by redesignating paragraph (7) as paragraph (8) and inserting after paragraph (6) the following:

"(7) The term 'physical evidence' means any object or device including any medical device, food product, drug, nutritional product, cosmetic product, or audio or video recording.".

(2) Section 20(c)(1) of the Federal Trade Commission Act (15 U.S.C. 57b–1(c)(1)) is amended—

(A) by inserting "physical evidence or" immediately after "any" the second time it appears;

(B) by inserting "to produce such physical evidence for inspection," immediately before "to produce";

(C) by inserting "physical evidence," immediately after "concerning"; and

(D) by inserting "evidence," immediately before "material, answers,".

(3) Section 20(c)(3) of the Federal Trade Commission Act (15 U.S.C. 57b–1(c)(3)) is amended—

(A) by inserting "physical evidence or" immediately before "documentary material";

(B) in subparagraph (A)—

(i) by inserting "physical evidence or" immediately before "documentary"; and

(ii) by inserting "evidence or" immediately after "permit such";

(C) in subparagraph (B), by inserting "evidence or" immediately before "material"; and

(D) in subparagraph (C), by inserting "evidence or" immediately before "material".

(4) Section 20(c)(10) of the Federal Trade Commission Act (15 U.S.C. 57b–1(c)(10)) is amended by inserting "physi-

cal evidence or" immediately before "documentary material" each place it appears.

(c) POSTAL DATA.—Notwithstanding any other provision of law, the United States Postal Service shall, within one hundred and eighty days after the date of enactment of this Act, amend its regulations in part 233 of title 39, Code of Federal Regulations, concerning mail covers to provide that the Federal Trade Commission may, in the course of investigating violations of law, use mail covers under the same procedures and to the same extent now permitted under other law enforcement agencies.

(d) FINANCIAL DATA.—Section 1109(a)(3) of Public Law 95-360, approved November 10, 1978, is amended—

(1) by redesignating subparagraph (E) as subparagraph (F);

(2) in subparagraph (D), by striking "or"; and

(3) by inserting immediately after subparagraph (D) the following new subparagraph;

"(E) dissipation, removal, or destruction of assets that are subject to forfeiture, seizure, redress, or restitution under any law of the United States by reason of having been obtained in violation of law; or".

(e) ASSISTANCE OF STATE ATTORNEYS GENERAL.—(1) The Commission may appoint State attorneys general to assist Commission attorneys to enforce Commission rules when the public interest so requires.

(2) Each person appointed under this subsection is subject to removal by the Commission at its discretion.

RULEMAKING ON TELEMARKETING

SEC. 5. (a) RULEMAKING.—Within two hundred and seventy days after the date of enactment of this Act, the Federal Trade Commission shall amend its rule in part 435 of title 16, Code of Federal Regulations, concerning mail order merchandise, to apply also to telemarketing. Except as specified in the remainder of this subsection, the amended rule shall apply to telemarketing to the same extent and in the same manner as it now applies to mail order sales.

(b) TELEMARKETING REQUIREMENTS.—As part of the rulemaking required by subsection (a) of this section the Commission shall consider including in the final rule a requirement that—

(1) each telemarketer shall inform the person, partnership, or corporation to whom the telemarketing is directed that such person, partnership, or corporation is entitled to a refund of any money paid for the product or service which is the subject of the telemarketing if delivery of the product or service is not made—

(A) within the time period included in the offer of the product or service, or

(B) if no time period is included in such offer, within thirty days after the date of the offer is made; and

(2) if such telemarketer—

(A) makes an unsolicited telephone call to a person, partnership, or corporation or otherwise communicates with such person, partnership, or corporation offering a free gift or prize and invites such person, partnership, or corporation to respond,

(B) a specific product or service is offered or sold in connection with such telephone call or other communication, and

(C) there is no Federal statute governing such telephone call or other communication involving such product or service,

such person, partnership, or corporation may cancel an order for such product or service not later than the expiration of three days after the date on which there is a sales agreement.

(c) Rebuttable Presumption.—Such amended rule shall include a rebuttable presumption that if a telemarketer does not keep adequate records to show compliance with the requirements described in subsection (b) of this section, such telemarketer shall be considered to be in violation of such requirement.

(d) LIMITATION.—For purposes of this section, a financial institution or other participant in a payment system used to pay for products or services offered or sold through telemarketing, including the credit or payment authorization aspect of such payment system, is not, by virtue of such participation, a telemarketer nor a person, partnership, or corporation which acts in concert with, or on behalf of, a telemarketer.

(e) DEFINITIONS.—For purposes of this section—

(1) the term "telemarketer" means a person, partnership, or corporation which engages in telemarketing; and

(2) the term "telemarketing" means the use of a telephone in the ordinary course of business to communicate with a person, partnership, or corporation an offer for sale or to complete a sale of a product or service.

LIFE CARE HOME STUDY

SEC. 6. (a) STUDY.—The Federal Trade Commission shall conduct a study of unfair or deceptive acts or practices in the life care home industry, including acts or practices engaged in by life care homes. Within twenty-four months of the date of enactment of this section, the Commission shall report the findings and conclusions of the study to Congress.

If the Commission finds a rulemaking is warranted under section 18 of the Federal Trade Commission Act, the Commission shall, promptly after completion of the study, initiate a trade regulation rule proceeding under such section 18 respecting unfair or deceptive acts or practices in the life care home industry. If the Commission determines a rulemaking is not warranted, the Commission shall include in the report to Congress the reasons for such determination.

(b) DEFINITIONS.—For purposes of subsection (a)—

(1) the term "life care home" includes the facility or facilities occupied, or planned to be occupied, by residents or prospective residents where a provider undertakes to provide living accommodations and services pursuant to a life care contract, regardless of whether such facilities are operated on a profit or nonprofit basis; and

(2) the term "life care contract" includes a contract between a resident and a provider to provide the resident, for the duration of such resident's life, living accommodations and related services in a life care home, including nursing care services, medical services, and other health-related services, which is conditioned upon the transfer of an entrance fee to the provider and which may be further conditioned upon the payment of periodic service fees.

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II

100TH CONGRESS
2D SESSION

H. R. 4101

IN THE SENATE OF THE UNITED STATES

JULY 6, 1988

Received; read twice and referred to the Committee on Commerce, Science, and Transportation

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AN ACT

To amend the Federal Trade Commission Act to strengthen the authority of the Federal Trade Commission respecting fraud committed in connection with sales made with a telephone.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE: REFERENCE.

(a) SHORT TITLE.—This Act may be cited as the "Telemarketing Fraud Prevention Act of 1988".

(b) REFERENCE.—Except as otherwise specifically provided, whenever in section 2 an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Federal Trade Commission Act.

SEC. 2. COMMISSION AUTHORITY.

The Federal Trade Commission Act is amended by redesignating sections 24 and 25 (15 U.S.C. 57c, 58) as sections 25 and 26, respectively, and by adding after section 23 the following:

"SEC. 24. (a)(1) The Commission shall promulgate rules for the telemarketing activities of a person, partnership, or corporation. In promulgating such rules, the Commission shall consider the inclusion of—

"(A) a requirement that products or services offered by telemarketing be shipped within a specified period and that if the products or services are not shipped within such period a refund be required,

"(B) authority for a person who orders a product or service through telemarketing to cancel the order within a specified period,

"(C) restrictions on the hours of the day when unsolicited telephone calls can be made to consumers, and

"(D) recordkeeping requirements.

"(2) Any person, partnership, or corporation which violates any rule promulgated under paragraph (1) shall be considered to have engaged in an unfair or deceptive act or practice in or affecting commerce.

"(3) The Commission shall promulgate the rules under paragraph (1) within 180 days of the date of the enactment of this section and in accordance with section 553 of title 5 of the United States Code.

"(b) A person, partnership, or corporation which engages in telemarketing may not engage in any conduct the natural consequence of which is to harass, oppress, or abuse any person in connection with the telemarketing, including conduct which involves—

"(1) the use or threat of the use of violence or other criminal means to harm the physical person, reputation, or property of any person,

"(2) the use of obscene or profane language or language the natural consequence of which is to abuse the hearer or reader, or

"(3) the placement of telephone calls without meaningful disclosure of the caller's identity.

A person, partnership, or corporation which engages in such conduct shall be considered to have engaged in an unfair or deceptive act or practice in or affecting commerce.

"(c)(1) Any attorney general of a State and any other official of a State vested under State law with the authority to enforce State consumer protection laws may bring a civil action in the name of the State in a district court of the United States having jurisdiction of the defendant to secure relief, as provided in paragraph (3), against any person, partnership, or corporation which engages in telemarketing which is a fraudulent act or practice or which violates the rule promulgated pursuant to subsection (a) if the attorney general or other official alleges that such telemarketing affects the State or its residents.

"(2) No action may be commenced under paragraph (1) unless the Commission has been given written notice of the commencing of the action—

"(A) at least 30 days before the action is to be commenced, or

"(B) as early as practicable if the attorney general or other official commencing the action—

"(i) alleges that the harm to the public is ongoing or presents an imminent hazard, and

"(ii) petitions the court for temporary or preliminary relief from such harm.

The Commission may intervene, by its own attorneys, in any such action, and the attorney general or other official of another State may intervene in any such action if the State or its residents are affected by the telemarketing with respect to which the action is brought.

"(3) In an action brought under paragraph (1) a court may grant such relief as the court finds necessary to redress injury to consumers or other persons, partnerships, and corporations resulting from the telemarketing for which the action is brought. Such relief may include—

"(A) rescission or reformation of contracts,

"(B) the refund of money or the return of property,

"(C) the payment of damages,

"(D) public notification respecting the telemarketing involved in the action, and

"(E) injunctions.

An attorney general or other official of any State may petition any court which has jurisdiction of a person, partnership, or corporation subject to an order of a court granting relief to enforce such order with respect to such person, partnership, or corporation if the attorney general or other official alleges that failure to comply with such order affects such State or its residents.

"(4) For purposes of this section—

"(A) the term 'attorney general' means the chief legal officer of a State, and

"(B) the term 'State' includes the District of Columbia.

"(d)(1) Any person, partnership, or corporation may commence a civil action to secure relief, as provided in subsection (c)(3), against a person, partnership, or corporation which engages in telemarketing which is a fraudulent act or practice or which violates the rule promulgated pursuant to subsection (a) if the amount in controversy exceeds the sum or value of $10,000. Such an action may be brought in a district court of the United States having jurisdiction of the defendant.

"(2) No action may be commenced under paragraph (1) unless the Commission has been given written notice of the commencing of the action at least 30 days before the action is to be commenced.

"(3)(A) The Commission may intervene, by its own attorneys, in any such action.

"(B) The court, in issuing any final order in any action brought under paragraph (1), may award costs of suit and reasonable fees for attorneys and expert witnesses if the plaintiff prevails.

"(C) Nothing in this subsection shall restrict any right which any person, partnership, or corporation may have under any statute or common law to seek enforcement of this Act or any rule or order under this Act or to seek any other relief.

"(e) For purposes of this section—

"(1) a financial institution or other participant in a payment system used to pay for products or services offered or sold through telemarketing, including the credit or payment authorization aspect of such payment system, is not, solely by virtue of such participation, a person, partnership, or corporation which engages in telemarketing or acts in concert with, or on behalf of, a person, partnership, or corporation which engages in telemarketing, and

"(2) the term 'telemarketing' means the use of a telephone in the ordinary course of business to communicate with a person an offer for sale or to complete a sale of a product or service.".

SEC. 3. CLEARINGHOUSE.

The Federal Trade Commission shall establish a clearinghouse for inquiries made to Federal agencies concerning telemarketing (as defined in section 24(e)(2) of the Federal Trade Commission Act). The clearinghouse will provide information (other than information which may not be disclosed under section 552(b) of title 5 of the United States Code) to anyone making inquiries respecting persons, partnerships, or corporations engaged in telemarketing or direct such inquiries to the appropriate Federal or State agency.

SEC. 4. STUDY OF COMPUTER CALLS.

The Federal Trade Commission, in consultation with the Federal Communications Commission, shall conduct a study of telemarketing telephone calls which are generated by computers. In conducting the study, the Commission shall—

(1) determine the hours of the day in which such calls are made,

(2) determine if such calls unduly harass the individuals called, and

(3) determine the effect of the inability of the individual called to terminate such calls.

Not later than 12 months after the date of the enactment of this Act, the Commission shall report to the Committee on Energy and Commerce of the House of Representatives and the Committee on Commerce, Science, and Transportation of the Senate on the results of the study under this section together with recommendations.

Passed the House of Representatives June 28, 1988.

Attest: DONNALD K. ANDERSON,

Clerk.

Senator GORE. Our first witness is Hon. Thomas A. Luken from the U.S. House of Representatives, a personal friend, the chairman of our counterpart subcommittee in the House and the sponsor of H.R. 4101. Again, our apologies, Congressman Luken; and I know that you are on a busy schedule and we appreciate you appearing here. Please proceed.

STATEMENT OF HON. THOMAS A. LUKEN, U.S. REPRESENTATIVE FROM OHIO

Mr. LUKEN. Thank you, Senator Gore, Senator McCain.

It is a pleasure to be here to testify before a former colleague and a very good friend and before this respected panel. Much of what I have to say, you gentlemen have very expertly and eloquently covered in your statements.

This is a very important piece of legislation. I think basically what it does is allow the law to catch up with the technology and the ingenuity of the schemers who have been contriving new types of scams in recent years.

Legitimate telemarketing, however, does exist, and it is a $100 billion a year industry. But telemarketing fraud is a blight on this industry, and we as members of Congress can do something about it in the form of the legislation that is proposed.

Perhaps I could be most useful to you by sharing with you some of the things we learned as the subcommittee dug into the problem of telemarketing fraud at our first hearing over a year ago. We then realized that telemarketing fraud was not limited to travel scams, though they are a large piece of the problem, and the elderly are especially vulnerable to them.

At our second hearing last December, we had witnesses who were also the victims of telemarketing fraud involving office supplies and vitamin pills. I will refer a little bit more to that later.

But it is surprising, I think, to many people that office personnel, people in the business world, not just the little old ladies and others who might pick up the phone rather sleepily some evening, are being duped. People who are supposed to be sophisticated and working in offices have been taken in scams involving hundreds of millions of dollars.

In early March we introduced, as a result of these revelations, the Telemarketing Fraud Prevention Act of 1988, H.R. 4101. And soon thereafter, Mr. Chairman, an identical bill was introduced by you in the Senate.

In April Senator McCain introduced the Consumer Fraud Prevention Act, S. 2336. While that bill dealt with several issues other than telemarketing fraud, as he has indicated, section 5 of Senator McCain's bill is based on the section of H.R. 4101 and S. 2213 that deals with the telemarketing rule, which is the basis of the legislation we have been working on.

There is a bipartisan recognition, Mr. Chairman, that telemarketing fraud is a large problem and that current law enforcement structures do not meet the needs. In the House Mr. Whittaker, the ranking Republican on our subcommittee, was an original co-sponsor of the bill and it had bipartisan support.

The bill did pass the House, as you have indicated, and was supported—I think it is important to give the litany of these impressive organizations—by the National Consumers League, the MasterCard, Visa, the National Office Machine Dealers Association, National Tour Association, the American Society of Travel Agents, and the National Association of Attorneys General, and others. But those are ones that are very pertinent to this legislation and endorsed it.

The need for legislative reform can be shown by looking at the packet of telemarketing fraud materials that the FTC sent over last month to the congressional press secretaries. Much of this information is also in the Commission's testimony.

The material says that telemarketing fraud is costing American consumers about one billion dollars, and I have seen estimates as high as $20 billion. The FTC materials also state that since 1982 the FTC has brought 29 Federal court actions and has recovered $23 million for consumers.

That means the FTC is recovering for consumers less than one percent of what they are losing. Moreover, $15 million of what the FTC has actually recovered, more than half of what it has actually recovered, was obtained in one single action.

In other words, in cases brought since 1982 the FTC has gotten back only $8 million for consumers. As a former Federal prosecutor, I think that record is pretty poor.

The victims of telemarketing fraud are not impressed by the FTC's performance any more than are we, and they want Congress to act.

Meanwhile, the states, using state law, are also going after fraudulent telemarketing. The National Association of Attorney Generals told the subcommittee that in 1987 the states had brought over 100 telemarketing cases. But each state, using state law, can only get relief in its own state for its own citizens.

Let me illustrate the problem The FTC tells us that it sued Mytel International in Federal court in the fall of 1987 over an office supply scam. Yet North Carolina had already obtained an injunction against Mytel in 1984 and Illinois had obtained an injunction against Mytel in early 1987.

But neither of these two states, which relied on state law, could get a national injunction, and the FTC investigated Mytel for three years before it sued.

Let us give one more example. The FTC sued Amy Travel in Federal court in August of 1987 for a travel scam. But six states, Illinois, Indiana, and others, had each already sued Amy in 1987.

Thus, the states can frequently move quickly against fraud, quicker than the FTC. But states, relying solely on state law, cannot get the same relief that the FTC can get. Our bill solves this problem and helps avoid duplicative state and Federal investigations.

Encouraging a state to sue in Federal court under Federal law will also reduce the risk of inconsistent decisions by state courts applying state laws, since in the Federal court system the courts of appeals can ensure that the Federal courts in different states apply the law in a uniform manner.

Having both the states and the Federal agency enforce the Federal law is used, I hasten to add, for example by the CFTC in its attack on fraud and by others. NHTSA uses this kind of procedure also. As a matter of fact, the CFTC in its attack on fraud issued a letter, and I ask that that letter of December 16th, which accompanies my statement, would be submitted in your record.

Senator GORE. Without objection, it will be included by reference.

Mr. LUKEN. And this letter says that permitting the states to enforce the Commodity Exchange Act in Federal court has helped the CFTC to enforce the statute.

Finally, Mr. Chairman and Senator McCain, a combination of Federal, state, and private enforcement of Federal law is also used in combating odometer fraud, antitrust laws, and some environmental laws, such as the Solid Waste Disposal Act and the Noise Control Act.

In conclusion, a combined Federal, state, and private attack on telemarketing fraud will bring quicker and more effective enforcement, save scarce Federal dollars, and provide more uniformity in enforcement. And I think there is a clamor out there on the part of consumers, which you, Senator, have noted, and I hope that we working together can get legislation through this Congress.

Senator GORE. I sure hope so, too. We are going to do our best.

When you looked at your bill in committee, you amended it to permit the FTC to set forth the specifics of the telemarketing rule, rather than attempting to specify mandatory elements in the bill itself. Why did you adopt that course?

Mr. LUKEN. Senator Gore, we thought that it might be too detailed and the legitimate retailers, retail organizations, also advised us that that was their opinion. So we did it partly out of our own lights, but also because we were so advised by those who are in the field.

Senator GORE. Now, in passing the bill did you find that members of the House from across the country identified telemarketing fraud as a significant problem, or did you notice it to be regional in nature?

Mr. LUKEN. Senator, I think that this is a real universal problem, and it is recognized as such, and we had that feeling from hearing from members. There has been a great deal written on the subject. The clippings must be deep, several inches thick, if we had them all here.

I have had quite a number of conversations, not only with other members, but with media representatives from around the nation. They are very concerned about it and they have written extensively on it, and I think almost uniformly in support of the kind of legislation that we are both working on.

Senator GORE. I have got some other questions that I will submit for the record and if at your convenience you and your people could respond to them, I would appreciate that.

I will recognize Senator McCain now.

Senator MCCAIN. I have no questions, Mr. Chairman. I would like to thank our friend, Congressman Luken, for his hard work and very fine product that he has brought before us today. We thank you.

Mr. LUKEN. Thank you.

Senator GORE. I would like to say before you go, Tom, that I want to applaud your leadership in behalf of consumers and the legitimate business people in this area. You have really been a great leader on this issue and we appreciate the chance to work with you.

Thank you.

Mr. LUKEN. Thank you, Senator.

Senator GORE. Our next witness is Hon.Terry Calvani with the Federal Trade Commission. We had invited the Chairman and he could not attend. We are very pleased to have Commissioner Calvani.

When I was a very young law student, he was the senior professor at Vanderbilt Law School, and I am delighted to have a chance to have him testify again before this subcommittee.

STATEMENT OF TERRY CALVANI, MEMBER, FEDERAL TRADE COMMISSION

Mr. CALVANI. Mr. Chairman, I thought you were one of the few students that was older than I was at the time.

Senator GORE. Without objection, your entire statement will be included in the record. Please proceed as you see fit.

Mr. CALVANI. Thank you.

Mr. Chairman, members of the committee, I am delighted to be here this afternoon to visit with you about the important subject of telemarketing fraud and the bills that are currently before this subcommittee.

Our time is limited. Accordingly, I would like to forego my prepared submission on behalf of the Commission and instead focus on the differences between S. 2326 and S. 2213.

S. 2326, introduced by Senator McCain, is in my view a very important piece of consumer protection legislation that very significantly expands the jurisdictional reach and power of the Federal Trade Commission.

First, S. 2326 substantially enhances proper venue in Commission-initiated proceedings. S. 2213 contains a similar venue provision, except that it expands proper venue for section 19. In other words, one bill focuses on section 13, the other on section 19; and here is the rub.

Most all of our telemarketing cases are brought pursuant to section 13. In fact, I cannot recall a single telemarketing case brought pursuant to section 19, nor, the way that sections 13 and 19 are crafted, is it likely that we would ever bring an action pursuant to section 19 to seek any kind of equity relief.

Thus, 2326 significantly enhances our enforcement powers. S. 2213 does not.

Second, 2326 would permit the Commission to use mail covers in the course of its investigations. This would assist us in locating victims, and it would assist us in locating potential witnesses. It would also assist us in locating assets for possible consumer redress.

Thus, 2326 adds yet another weapon to our arsenal. 2213 does not.

S. 2326 permits the Commission to compel the production of physical property. Current law limits pre-complaint discovery to the production of documents or testimony. By allowing the Commission to compel the production of physical property, this bill provides us yet another enforcement weapon. S. 2213 does not.

S. 2326 would amend the Right to Financial Privacy Act to permit the Commission to delay notice to individuals when obtaining access to their financial records if there is reason to believe (to the satisfaction of a Federal judge) that such notice would result in the dissipation of assets subject to redress or restitution.

S. 2326 provides yet another enforcement weapon. 2213 does not.

In summary, several provisions of 2326 just mentioned provide a wide array of new enforcement weapons to the Commission. 2213 does not.

Lastly, I should like to address the creation of the private right of action and delegation to state attorneys general that are treated in the three bills. First, I have grave reservations about the wisdom of enacting another RICO statute. Everyone in this room and certainly you gentlemen on the dais are quite familiar with the controversy that has surrounded the RICO statute.

H.R. 4101 and S. 2213 will, like RICO, federalize common law wire fraud. Under these bills, you may have a new Federal cause of action if you believe that you have been misled on the phone.

I urge you at a minimum to consider the wisdom of this section in light of the voluminous record on this general subject put together by the respective Judiciary Committees of both houses of Congress. Although the courts have to some extent tightened the use of RICO, much garden variety business fraud litigation is now in the Federal courts.

Under this mini-RICO statute, a disagreement between a business person and her investment advisor, her broker, as to the appropriate depreciation schedule on a real estate investment would be federalized if the alleged misrepresentation were made by phone.

Indeed, 2213 would appear to be more expansive than the present RICO statute, since it does not contain the enterprise and pattern requirements of current law. At a time when the committees of Congress are considering substantive RICO reform, query whether this committee wants to sire Son of RICO.

I urge you to visit also with Chairman Biden, Chairman Rodino, and their respective committees. I think they have given a lot of thought to these issues.

Frankly, I doubt that this provision would be of much benefit to consumers. Private lawsuits are impractical for most telemarketing victims, given the amount of damages vis a vis the cost of litigation.

Now let us turn to the general subject of delegation to state attorneys general. S. 2326 goes a very long way toward furthering Federal-State consumer protection cooperation. It is very important to note that 2326 permits the deputization of State authorities to enforce any Commission rule.

S. 2213 and its companion H.R. 4101, while expanding this authority in some sense, limit it to telemarketing issues. So 2326 is far more expansive and permits the Commission to deputize enforcement of all its 36 rules, including the used car rule, funeral rule, et cetera.

More importantly, the constitutionality of S. 2213 is in my view at least cloudy. It is and will be argued that only officers of the United States may enforce Federal law and that State officials cannot discharge these responsibilities consistent with Article II, section 2, clause 2 of the United States Constitution, the so-called appointments clause.

I call to your attention the statement of the President of the United States of May 19, 1988, in signing the Appalachian States Radioactive Waste Compact and the correspondence between Senator Joseph Biden and Assistant Attorney General John Bolton with reference to that legislation. I believe you have been furnished copies of all of that.

Gentlemen, I am not a constitutional scholar and I do not pretend to be, and I have, quite honestly, no earthly idea whether the courts would ultimately find this constitutional or not. But there are two important issues that you ought to consider.

First, does the President's statement of May 19 lead you to believe that S. 2213 risks a presidential veto or, at a minimum, a statement by the President doubting the constitutionality of the provision?

And secondly, will not the enforcement of 2213, if passed and signed, be a lawyer's dream, since the constitutionality will certainly be tested in every circuit? Indeed, it would probably be malpractice for counsel representing a defendant in a state-initiated proceeding not to raise the issue.

You then have, I submit, a clean bill and one—and I am not going to say that it is unconstitutional, but at least that raises constitutional issues, before you.

One last comment. I am concerned that the provisions within S. 2213 with reference to the establishment of a clearinghouse may well frustrate law enforcement efforts. Most inquiries would probably seek information as to whether a participating telemarketer is under investigation. Such information, if provided to the targets of the investigation, rather obviously could jeopardize law enforcement efforts. It does not take much imagination to envision operators of certain scams disappearing overnight on learning that they are subjects of such investigations.

The Commission staff is currently working with State law enforcement officials in order to establish a clearinghouse that would accomplish the legitimate objective of sharing information from State law enforcement agencies, but without the defect that I described in S. 2213.

In conclusion, I and my colleagues endorse S. 2326 as an important expansion of the Commission's jurisdiction and authority to prosecute telemarketers. We have, however, significant reservations about S. 2213 and its companion House bill.

Thank you for your time and indulgence, Mr. Chairman. I would be happy to respond to your questions.

Senator GORE. Very good. I am going to try to hold my questions to a shorter than usual period because we started so late, and then perhaps you would be willing to respond in writing to some additional questions for the record?

Mr. CALVANI. I would be delighted, Mr. Chairman.

Senator GORE. First of all, has the FTC increased its resources allocated to combatting telemarketing fraud?

Mr. CALVANI. No, Mr. Chairman, the FTC has not increased its resources.

Senator GORE. According to information provided by the Commission to the subcommittee, the FTC's consumer protection mission has been slashed from 530 work years in FY 1981 to 349 work years in FY 1988. However, the percentage of those reduced resources allocated to telemarketing fraud has risen during that time so proportionately more resources are allocated to it.

Mr. CALVANI. That may well be true, but our budget has been going down in real terms, as you are doubtless well aware, over a good number of years.

Senator GORE. And the internal allocations to consumer protection, if I am not mistaken, have also been cut rather significantly.

You say that you have brought 29 federal court cases against telemarketers in the last five years. Given the fact that telemarketing fraud is now costing consumers a billion dollars per year, does not six cases a year seem like a small number for a billion dollar rip-off?

Mr. CALVANI. Well, Mr. Chairman, I think it depends—small is a relative term. Obviously it is small in terms of the total number of cases of fraud that are perpetrated on consumers. The question is really use of the resources that the Commission has. There are lots of areas over which we have jurisdiction where the presence in absolute numbers is small. It is a question of balancing the resources available to the Commission.

Senator GORE. And the smaller amount requested by the administration for that task taken together, all of those points seem to argue in favor of searching out other ways to have the law enforced, particularly if a billion dollars a year is being lost.

Now, the main avenue under the FTC Act used by the FTC is section 13, correct?

Mr. CALVANI. That is correct, sir.

Senator GORE. It offers injunctive relief.

Mr. CALVANI. That is its principal asset to us.

Senator GORE. Other sections require some kind of prior administrative action and therefore it results in slower action, is that right?

Mr. CALVANI. That is correct.

Senator GORE. Now, let me ask you about the idea in Senator McCain's bill of deputizing Attorneys General. How would you envision that working, on a case-by-case basis or on an across-the-board basis?

Mr. CALVANI. I think we would need to work closely with the National Association of Attorneys General sorting that through. As you know, Senator McCain's bill would provide deputization for the enforcement of any or all Commission rules. There are probably some rules where it would be appropriate to grant blanket deputization and others that you might want to do on a case-by-case basis. But quite honestly, I think I would want to consult with my good friends at the National Association and work together with coming up with a protocol on that.

Senator GORE. We will be hearing from them next. There is no precedent for the FTC doing that that you are aware of, is there?

Mr. CALVANI. Not that I am aware of.

Senator GORE. How successful is the computer system regarding telemarketing fraud jointly operated by the FTC and the Attorneys General?

Mr. CALVANI. Mr. Chairman, it is probably too early to tell because it is a reasonably new development. There are some 22 different states that have been active participants, according to the information that has been provided to me. There are a good number of states that are not currently participating. It is a reasonably new effort. A year from now we could probably give you a better answer.

Senator GORE. Now, you stated that amending the mail order rules as provided in the McCain bill is unlikely to address the practices that characterize telemarketing fraud. Why is that so?

Mr. CALVANI. Well, Mr. Chairman, I do not oppose that provision. It may add something. But the fact of the matter is that most of the perpetrators of telemarketing fraud are not guilty of the kinds of practices that led to the mail order rule. The problems that led to the mail order rule were where you ordered something and it did not show or it showed up six months later. Most of the problems that we confront with reference to telemarketing involve your basic garden variety of thievery. It is not a question of not getting it on time.

Senator GORE. Something shows up, but it is not right.

Mr. CALVANI. Most of these cases are cases against criminals, which leads me to one personal comment, and I speak for no one other than myself. At some point it might be a good idea for us to talk about granting to the Commission criminal law enforcement power in this area because unless these individuals start serving time we are not going to see much significant rollback over the long term.

I think Senator McCain's bill provides us additional weapons. We will be more effective if that bill is enacted, but we are really using civil law enforcement techniques to go after criminal conduct.

Senator GORE. But the particular scams involved here do not usually lend themselves to the authority that we have in the mail order rule simply because of the way they operate.

You mentioned that the FTC has streamlined its investigative and deliberative procedures regarding telemarketing so that a complaint is filed now within six to seven months of the beginning of the investigation. What used to be the time period?

Mr. CALVANI. It was much longer, Mr. Chairman, but I do not have those numbers at my fingertips.

Senator GORE. If you could provide that for the record.

Mr. CALVANI. I would be delighted.

[The information referred to follows:]

TELEMARKETING FRAUD CASES FILED BY FTC SINCE DECEMBER 1982

Case name	Year filed	Number of defendants	Judgment (millions)	Year ordered	Distributed to consumers	On deposit in bank	Held by receiver	Case type
1 Alaska land leasing	1984	11	2.000	1987		2.000		Investment.
2 Any Travel Service Inc	1987	5	6.600	1988				Vacation Trips.
3 ANC	1985	6	1.000	1986			1.000	Investment.
4 Atlantex	1986	9	12.175	1987				Do.
5 Beverly Hills Coin Gallery.	1988	6					(1)	Do.
6 Bliss Holidays International Inc.	1988	3						Vacation Trips.
7 Copydata	1985	2	.300	1987	.300			Office Supplies.
8 Federal Sterling Galleries.	1987	4						Investment.
9 First Petroleum	1982	4	.125	1983	.125			Do.
10 J&R Marketing	1984	7	.700	1985				Do.
11 Kimberly	1983	9	.266	1985	.266			Do.
12 Leland	1983	8	2.500	1985	2.500			Do.
13 Lynn Murphy Co., Inc.	1988	4						Do.
14 Mytel International Inc.	1987	3						Office Supplies.
15 Nationwide Printing	1988	2						Advertising Specialties.
16 North American	1985	7	.060	1987				Office Supplies.
17 Numismatic Enterprises, Inc.	1987	5						Investment.
18 Overseas Unlimited Agency, Inc.	1988	3						Overseas Employment.
19 Rare coin galleries	1986	5						Investment.
20 Schoolhouse Coins/ Numis Group.	1987	8						Do.
21 Security rare coin	1986	3						Do.
22 Southwest Marketing, Inc.	1988	4	.075	1988				Advertising Specialties.
23 Standard financial	1984	3	1.500	1987		1.500		Investment.
24 TCC	1985	6	.100	1985	.100			Do.
25 Trans-Alaska	1983	12	2.176	1987				Do.
26 Travel World International.	1988	4						Vacation Trips.
27 U.S. oil and gas	1983	13	51.265	1987			15.000	Investment.
28 Volcano mines	1986	5	.065	1986		.065		Do.
29 World Travel Vacation Brokers, Inc.	1987	4						Vacation Trips.
		165	80.907		3.291	3.565	16.000	

[1] Unknown.

Note.—The 29 companies listed had, at the time of suit, estimated sales of 624.4 million dollars. An estimated 1,113,500 consumers were victimized by these firms.

Senator GORE. Well, I have one final question. When the House passed H.R. 4101, it deleted the standard "dishonest" with regard to the requirement for bringing an action against violators of the act, and instead the bill relies simply on fraudulent acts. Is this a good idea? Is the standard clear? What do you think?

Mr. Calvani. Mr. Chairman. I would rather respond to that question in writing. I get in trouble when I start talking about something I do not know anything about. and that would fall in that category.

Senator Gore. Yes. I know that, Commissioner. So do I.

Senator Gore. Senator McCain.

Senator McCain. Thank you. Mr. Chairman. I would like to congratulate you, Commissioner Calvani, on the superb job you did in training Senator Gore.

Mr. Calvani. I only take credit for part of it.

Senator Gore. He came up with my entire electoral strategy in New York also.

Senator McCain. From a nonpartisan viewpoint. I hope he is available for your reelection.

Senator Gore. Now, be careful. I spoke well of your bill.

Senator McCain. In the interest of time——

Senator Gore. That is all right. I understand.

Senator McCain. Mr. Chairman—thank you, Commissioner. and first of all could I express my appreciation for the efforts and cooperation that I have received from the Commission and your staff and the dedication that I have seen on the part of the Commission to try to address this very difficult issue. It was a privilege for me to come and testify before the Commission some months ago. and I think that we can and will work very closely in addressing this incredibly serious issue.

In my opening statement. I was trying to come up with some concrete examples because this issue needs to be humanized. When I testified before the FTC, I had a gadget with mirrors and lenses that was a supposed cure cancer. The person who received that gadget later died of cancer. These things are worse than rip-offs in many cases, particularly where the elderly are concerned. That is why I think we need to give some concrete examples of how serious this issue is. It just is not a matter of money.

In your testimony, I think you said that section 13 is basically the only section that is used for the enforcementagainst consumer fraud because section 19 is just too cumbersome—is that correct?

Mr. Calvani. Yes, Senator, section 13 permits us to go into court and seek immediate equitable relief. Under section 19 as the chairman has just indicated, there must be either a rule violation or a prior administrative proceeding. And so, obviously, if you are dealing with somebody as slippery as most of the respondents that we confront in the telemarketing area, they are going to be long gone by the time we get around to section 19.

Senator McCain. Do other agencies have the authority to appoint state officials for federal court proceedings, do you know?

Mr. Calvani. Yes, Senator. In thinking about the constitutional issue, I have had occasion to review a good number of statutes and a lot of cases. A wide variety of delegation and deputization schemes are used.

Senator McCain. You mentioned in response to one of Senator Gore's questions that 22 states are participating in the cooperative telemarketing data bank. Why are a majority of the states in your opinion not participating?

Mr. CALVANI. Senator, I do not know. That question had best be asked of Attorney General Stephan. But my guess is it is a new program, and like all new programs it takes time to get into place, but I would defer to his good judgment on that question.

Senator MCCAIN. Do you have any idea how many states in the past have asked the FTC to initiate litigation concerning telemarketing fraud?

Mr. CALVANI. A good number. Recently we have had some sterling successes in working with state authorities in this area, but I do not have a precise numerical answer to your question.

Senator MCCAIN. Have these requests increased as the visibility concerning telemarketing fraud increased?

Mr. CALVANI. Well, I think so. It is probably due in some measure to the cooperative efforts associated with the clearinghouse.

Senator MCCAIN. In contrast the FTC, which we all know only has authority to initiate civil actions against these individuals and companies, many states can initiate criminal actions against telemarketing con artists. How effective are such criminal sanctions?

Mr. CALVANI. Well, I think they ought to be more effective than any of the civil remedies. Quite honestly, Chairman Gore made reference earlier to what appears to be, looked from afar as a spotty record in terms of returning dollars to injured consumers. But it is not surprising to me that the instant that we show up, we find the assets gone.

Now, do I actually believe that those assets have done up in the air? No, I do not think so in the least. I would be willing to bet you my dollar to your doughnut that we would find a lot of it in the Canary Islands and in Swiss bank accounts.

Not surprisingly when they are confronted with the reasonably small penalties that we have to offer, they simply decide to wait and in my judgment spend that money later on. I think when confronted with some time at a federal penitentiary, their memories would improve.

Senator MCCAIN. Amazing.

The House bill that was just described to us by the previous witness allows the 50 state AG's and local officials and private citizens unrestricted ability to bring suit in federal courts as I understand it. Have you any idea how many cases that would add to the federal caseload?

Mr. CALVANI. I think it would add substantial numbers, but most of them probably would not be the kind of telemarketing case that you and I have in mind. We have a vision in our mind of what is a telemarketing fraud perpetrator. But we are not able to draft a statute that addresses that problem that has a limiting principle that does not turn it into a new RICO statute. The bills before us, quite honestly, have the same problems and potential for abuse than the current RICO legislation. The problem with the private right of action is that it is going to end up federalizing common law wire fraud. And I do not think that is what the committee has in mind.

Secondly, with reference to the delegation issue, I think once again there is a clean bill and there is one that poses constitutional questions. I have no earthly idea what the courts are ultimately going to do, but as between a bill that is clearly constitutional and one where the President and the Justice Department, at least in another context, have had significant misgivings, I would opt for the clean bill.

Senator McCain. How does the Commission presently coordinate with the states on the issue of telemarketing fraud?

Mr. Calvani. Senator, it varies from case to case. Some of the investigations we have under way obviously involve locations in many states. And that is more complicated because you are trying to coordinate efforts with several law enforcement officers from several different states. So, it also depends upon who comes to whom first, who has found it first, and sort of an ad hoc agreement as to who is going to take the lead role. It does not make sense for everybody to reinvent the wheel. We have had some investigations where we have piggybacked on the back of state agencies, and we have had some that have worked vice versa, so it sort of depends upon the case.

Senator McCain. Thank you.

Thank you, Mr. Chairman.

Senator Gore. We may have additional questions in writing, and we certainly appreciate your appearance here today.

Mr. Calvani. Thank you, Mr. Chairman and Senator McCain.

[The statement follows:]

STATEMENT OF THE FEDERAL TRADE COMMISSION

Mr. Chairman and members of the Subcommittee: My name is Terry Calvani, and I am a Commissioner at the Federal Trade Commission. I appreciate this opportunity to appear before you today on behalf of the Federal Trade Commission to discuss our views on various legislative initiatives aimed at combatting telemarketing fraud.[1]

As you are aware, telemarketing fraud is a major problem for American consumers and one that causes substantial economic injury. We estimate that telemarketing scams may take as much as one billion dollars [2] a year out of the pockets of American consumers, ranging from widows looking for safe investments for insurance proceeds to business executives buying business equipment and supplies. Some commentators even claim that this estimate may be too conservative in view of the size of the telemarketing industry: Industry sources estimate that in 1986 alone, 118.5 billion dollars in sales were made over the telephone.[3]

Accordingly, for the past five years, combatting telemarketing fraud has been an important priority at the Commission. Our campaign has relied in part upon the aggressive prosecution of telemarketing scams. Since 1983, the Commission has brought 29 federal district court cases against nationwide telemarketing frauds with aggregate sales of over 624 million dollars.[4] Our actions have put over 165 individual and corporate telemarketers under federal court order, and we have obtained judgments for over 80 million dollars in redress for telemarketing victims. Of this amount, we have secured nearly 23 million dollars in redress for scam victims. This represents funds actually distributed to consumers, funds in the possession of FTC receivers and funds in bank accounts subject to FTC-obtained freeze orders. To date, more than 6,500 of those victims have received redress checks ranging from 50 dollars to 15 thousand dollars as a result of Commission actions.

Within the last five years, we have prosecuted telemarketing frauds involving the fraudulent sale of diamonds and other precious gemstones; [5] oil leases; [6] application preparation services for the Bureau of Land Management's lottery for oil and gas lease rights; [7] application preparation services for the Federal Communications Commission's lottery for cellular telephone licenses; [8] partnership shares in oil and drilling ventures; [9] silver and gold ore and ore processing; [10] rare coins; [11] offers of

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[1] While the views expressed in this statement represent the views of the Commission, my oral presentation and responses to questions are my own and do not necessarily reflect the views of the Commission or other individual Commissioners. Commissioner Strenio concurs in this statement and will forward additional views separately.

[2] This figure is based on industry information acquired by FTC staff developing telemarketing fraud cases. This figure is also consistent with remarks made by Senator Rudman during hearings before the Permanent Subcommittee on Investigations, United States Senate, on March 21, 1984.

[3] Industry Profile, 9 DM News 20, Oct. 15, 1987, at 8, 71 (quoting Kordahl and Fishman, Annual Guide to Telemarketing: 1986).

[4] We have attached a table to this statement listing the number of telemarketing cases that we have prosecuted, the number of defendants, the judgment amounts awarded and the amounts actually distributed to consumers.

[5] FTC v. Kimberly, Civ. No. 83-5268 JMI, (C.D. Cal.).

[6] FTC v. Alaska Land Leasing, Civ. No. 84-4516 AWT (Px), (C.D. Cal.); FTC v. Trans Alaska, Civ. 84-2001 AWT (Px), (C.D. Cal.).

[7] FTC v. U.S. Oil & Gas, 748 F.2d 1431 (11th Cir. 1984); FTC v. Leland, 83-3589 DVM (Px), (C.D. Cal.); FTC v. J&R Marketing, Civ. No. 83-1231 JE (S.D. Fla.); FTC v. First Petroleum, Civ. No. 82-2744 EPS (S.D. Fla.).

[8] FTC v. American National Cellular, Civ. No. 85-7375 WJR (Px), (C.D. Cal.); FTC v. The Cellular Corporation, Civ. No. 85-8231 WHO, (N.D. Cal.).

[9] FTC v. Atlantex, Civ. No. 87-0045 (S.D. Fla.).

[10] FTC v. Volcano Mines, Civ. No. 86-0340 (D. R.I.).

[11] FTC v. Security Rare Coin, Civ. No. 86-1067 (D. Minn.); FTC v. New England Rare Coin, Civ. No. 87-0330 WE (D. Mass.); FTC v. Rare Coin Galleries, 1986-2 (CCH) Tr. Cas. p 67,388 (D. Mass. 1986); FTC v. Schoolhouse Coins, Civ. No. 87-05415 KN (Px), (C.D. Cal.); FTC v. Beverly Hills Coin Gallery, Civ. No. 88-04645 KN (Ex) (C.D. Cal.); FTC v. Numismatic Enterprises Corp., Civ. No. 87-4045 LDW (E.D. NY); FTC v. Standard Financial, Civ. No. 87-0330 WF (D. Mass.).

"bargain" vacation packages in connection with the purchase of travel club membership;[12] business equipment and supplies[13] and employment services.[14]

Moreover, the Commission regularly monitors compliance with federal court orders that we obtain. Order violations are prosecuted as civil or criminal contempts depending upon the seriousness of the violations. To date, six criminal convictions for contempt of court have been obtained by Commission attorneys.

To prosecute telemarketing fraud successfully, we have revised our internal procedures and the manner in which we prosecute cases. Fraudulent telemarketers often operate for a limited period of time, disappear, then resurface later at a new address with another scam. To be effective, we have streamlined both our investigative and deliberative procedures. We now attempt to proceed from the opening of an investigation to the filing of a complaint within a 6–7 month period. But while this is a marked improvement over past efforts, we are working hard to cut this time down substantially. Fraudulent telemarketers often disappear or at least secrete their assets at the slightest hint that they are under law enforcement scrutiny. Consequently, we typically conduct our investigations without notifying the prospective defendants. For the same reason, we file our cases *ex parte* and seek asset freeze orders, which are served before defendants can withdraw assets from banks and other financial institutions. In the most egregious cases, we ask the court to appoint receivers to take physical control of defendant telemarketing businesses and operations to prevent the destruction of records and the dissipation of assets.

In addition to bringing our own law enforcement actions, the Commission works closely with state law enforcement officials to reduce the incidence of telemarketing fraud. The Commission believes strongly that the success of law enforcement in this area depends upon the degree of cooperation and coordination among all law enforcement agencies with jurisdiction over fraudulent telemarketers. Our cooperation with state authorities takes many forms. Perhaps the most significant step to date was our implementation of the automated databank on telemarketing fraud with the National Association of Attorneys General (NAAG) in the Fall of last year. This databank enables participating law enforcement agencies to use their collective data to identify the most serious violators, to gather evidence to prosecute those violators, and to identify recent trends in illegal activities for the purpose of planning the efficient allocation of law enforcement resources.

At present, the databank has 33 participants, including attorneys general or other state agencies in California, Connecticut, Florida, Illinois, Iowa, Kentucky, Massachusetts, Maine, Minnesota, Missouri, New Jersey, New Mexico, New York, Oregon, Pennsylvania, Tennessee, Texas, Vermont, Virginia, Washington, West Virginia and Wisconsin. Also included in the databank's membership are a number of federal agencies. It is the goal of NAAG and the Commission to bring the remaining states into the system.

Another important weapon that we have employed in the battle against telemarketing fraud is our consumer education program. Our activities in this are are designed to prevent consumers from becoming telemarketing victims. Our consumer education efforts include the production and distribution of thousands of "Consumer Alerts" on various forms of telemarketing fraud to consumers, reporters, and others who are in a position to inform the public about this problem and what they can do to protect themseleves.

Despite the Commission's best efforts, however, telemarketing fraud continues to be a serious problem. Given its sheer magnitude, we believe that neither the Commission nor any other single agency or office alone is capable of effectively deterring telemarketing fraud. To bring this problem under control, every state and federal law enforcement agency with jurisdiction over telemarketing fraud must commit itself to prosecuting all law violations to the full extent that the facts and law permit. In particular, those with authority to bring criminal actions must be willing to prosecute fraudulent boilerrooms operating within their jurisdiction, whether or not the scam's victims are located within their districts. We are convinced that only the threat of incarceration will deter some of the most egregious perpetrators of telemarketing scams.

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[12] FTC v. Amy Travel Service, Civ. No. 87-6776 (N.D. Ill.); FTC v. World Travel Vacation Brokers, Civ. No. 87-8449 (N.D. Ill.); FTC v. Blisss Holidays International, Inc., et al., Civ. No. 88-0397 (S.D. Fla.); FTC v. Discount Travel Service, Inc., et al., Civ. No. 88-113-Civ-FM-15C (M.D. Fla.).

[13] FTC v. North American Office Systems, Inc., et al., Civ. No. 3-86-1850-G (N.D. Texas, April 17, 1987); FTC v. Mytel International, Inc., et al., Civ. No. 87-07259-JMI-(GHKX) (C.D. Cal.); FTC v. Copy Data Systems, Inc., et al., Civ. No. 87-495-A (E.D. Va.); FTC v. Worldwide Factors Ltd., et al., CV-S-88-2293-RDF (D. Nev.); FTC v. Nationwide Printing, CV-S-88-293 RDF (D. Nev.); FTC v. Southwest Marketing, CV-S-88-458 RDF (D. Nev.).

[14] FTC v. Overseas Unlimited Agency, Inc., Civ. No. 88-2583 WJR (Gx) (C.D. Cal.).

Of course, civil law enforcement agencies must be equally aggressive in attacking telemarketing scams. Civil actions can stop frauds quickly and return captured assets to victims. As a result, we are pleased to offer our views on the three legislative initiatives that are designed to enhance the arsenal of weapons available to the Commission and others in the fight against telemarketing fraud through civil actions: Senate Bill 2213, a bill introduced by Senator Albert Gore; House Bill 4101, a bill which passed the House on June 28, 1988; and Senate Bill 2326, a bill introduced by Senator John McCain.

At the outset, we would like to commend Senators McCain and Gore, as well as Representative Luken, for their longstanding efforts on these important consumer protection issues. As Senator McCain pointed out recently during Commission-sponsored hearings on consumer problems affecting the elderly, additional legislation is needed to enhance the Commission's ability to protect all consumers from telemarketing abuses. The bills that they have introduced to combat telemarketing fraud reflect their genuine concern for and understanding of the problems consumers face.

SENATE BILL 2213

After examining the provisions in Senate Bill 2213, we must conclude that the bill is unlikely to enhance significantly enforcement efforts to reduce telemarketing fraud.[15]

First, the bill authorizes states to bring civil actions against fraudulent telemarketers under Section 19 of the Federal Trade Commission Act. We recognize that in some instances this provision may enhance states' ability to intercept fraudulent telemarketing schemes.[16] However, we believe that this approach may have unintended consequences that will outweigh these benefits.

Our principal concern is that enforcement of the FTC Act by states and, potentially, thousands of local district attorneys' offices,[17] may result in inconsistent application of the Act nationwide. Telemarketing cases are complex, involving a host of issues on which enforcement agencies reasonably may differ. In our telemarketing fraud program, we routinely confront difficult issues of deception law, scope of redress, the appropriateness of *ex parte* freeze orders, appointment of receivers, aiding-and-abetting doctrine, and others. As the number of agencies enforcing the Act increases, so too does the potential for inconsistent decisions.

Moreover, inconsistent law and adverse decisions may impact Commission enforcement outside the telemarketing area. In choosing cases and strategies, the Commission is best equipped to take into account the effect of precedent on issues affecting its other programs. One reason the Commission was established was to promote uniform application of antitrust and consumer laws to activities of commercial firms selling nationwide. The approach in Senate Bill 2213 at the very least will complicate the Commission's efforts in this regard.

Finally, we note some problems that may limit the potential benefits of this provision. The venue and service provisions governing district court suits may at times require that states file suit in distant jurisdictions, an expensive and complex undertaking. Moreover, we would hope that the bill would not result in a shifting of resources away from criminal prosecution, which, as we have said, is an important tool under existing state authority.

Second, the bill enables private citizens to sue fraudulent telemarketers under Section 19 of the Federal Trade Commission Act. Lawsuits may be impractical for many telemarketing victims unless the amount in controversy is relatively great, particularly where suit must be brought outside the victim's home jurisdiction.

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[15] Senate Bill 2213 is the companion bill to House Bill 4101, a measure previously considered by the House Subcommittee on Transportation, Tourism and Hazardous Materials, Committee on Energy and Commerce, U.S. House of Representatives, at a hearing on March 9, 1988. As Senate Bill 2213 is identical to the earlier version of House Bill 4101 that was considered at the hearing, we have attached a copy of the statement, along with the comments of individual Commissioners, that we submitted to the House Subcommittee detailing our views on some of the provisions contained in the earlier version of House Bill 4101.

[16] We should note that Senate Bill 2213 does not clearly give states injunctive authority. The provision authorizing states to bring civil actions is inserted in Section 19 of the FTC Act, which by its terms only authorizes redress. House Bill 4101, another bill under consideration by the Subcommittee, cures this ambiguity by granting states and private parties injunctive and other remedial authority under a new section to be created under the Federal Trade Commission Act.

[17] The bill grants authority to bring suit under Section 19 of the Act to "[a]ny attorney general of a State and any other official of a State vested under State law with the authority to enforce State consumer protection laws. * * *" We understand that there are thousands of local district attorney offices with such authority.

The private right of action provision also presents the same problems of inconsistent enforcement of the Act as discussed above. There has been considerable controversy over private plaintiffs' use of the Racketeer Influenced and Corrupt Organizations Act in litigation over garden-variety business disputes.[18] Similarly, Senate Bill 2213, containing broad definitions of "telemarketer"[19] and addressing undefined "fraudulent or dishonest act[s] or practice[s]," conceivably could be applied by private parties to actions outside the area of hard-core fraud the bill is intended to address. Conversely, we note that the telemarketing rule that the bill would require the Commission to promulgate, and which private parties could enforce, is unlikely to address the practices that characterize the typical telemarketing fraud.[20]

Third, to enhance the Commission's ability to combat telemarketing fraud, the bill would amend Section 19 of the Federal Trade Commission Act to permit the Commission to bring a telemarketing suit in one court against multiple defendants residing or transacting business in different districts. This provision is of particular interest to us, since we have experienced some difficulty in the past satisfying venue requirements where telemarketing scams involve action by individuals and firms scattered over several states.

Unfortunately, this provision would be of limited use to the Commission because most of the cases we bring against telemarketing scams are brought under Section 13(b) of the Federal Trade Commission Act rather than Section 19. Unlike Section 19, Section 13(b) permits the Commission to prosecute fraudulent telemarketing conduct and authorizes the Commission to seek injunctive relief.

Fourth, the bill would amend Section 19 of the Federal Trade Commission Act to prohibit telemarketing from harassing consumers. This provision appears to be modeled after those contained in the Fair Debt Collection Practices Act.[21] Generally, the telemarketing cases investigated by the Commission have not involved collection abuses. Consumers who call scam operators seeking to rescind a fraudulent transaction or to seek performance of a money-back guarantee may sometimes be subjected to verbal abuse. Although such abuse can cause considerable emotional distress, it is not the essence of the illegal activity, nor is it the primary source of injury in these cases. This provision, therefore, would not appreciably assist the Commission in its efforts to prevent telemarketing fraud. In addition, this provision provides no guidance for those empowered to enforce it in the form of examples of prohibited conduct. Examples of collection abuses described in the Fair Debt Collection Practices Act have assisted the Commission in enforcing that Act.

Finally, the bill would require the Commission to provide information to any person inquiring about telemarketers through a clearinghouse to be established by the Commission. Based on our experience, we believe that most persons who would make such inquiries would want information on whether a particular telemarketer is under investigation by the Commission or whether any complaints have been made against the company. The Commission cannot always disclose this information, however, without jeopardizing its ongoing investigations. For example, operators of telemarketing scams are likely to secrete their assets or disappear overnight upon learning that they are the subject of a Commission investigation.

For the foregoing reasons, we believe that Senate Bill 2213 is unlikely to be of significant assistance to states and private parties in the fight against telemarketing fraud. Moreover, the bill, as presently drafted, adds little to the Commission's enforcement authority and could even endanger the Commission's existing ability to combat telemarketing scams.

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[18] 18 U.S.C. 1961 (1982 & Supp. IV 1986).

[19] Section 2(g) of the bill defines "telemarketing" as "the use of a telephone in the ordinary course of business to communicate with a person an offer for sale or to complete a sale of a product or service."

[20] Under Senate Bill 2213, the Commission would be required to promulgate a telemarketing rule modeled after the Mail Order Rule, 16 C.F.R. 435 (1987), currently enforced by the Commission. The Mail Order Rule is designed to address problems with delayed delivery of ordered merchandise. Shipping delays, however, are not the essence of telemarketing frauds. Rather, these cases generally involve misrepresentations regarding the nature, value, quality, or cost of the products or services sold. In addition, the cooling-off provision in the proposed rule would not affect the vast majority of fraudulent telemarketing transactions, because the consumer typically is unaware that he or she has been defrauded until long after the initial transaction.

[21] 15 U.S.C. 1601 (1982 & Supp. IV 1986).

HOUSE BILL 4101

House Bill 4101 is the companion bill to Senate Bill 2213. As amended and passed by the House of Representatives, the bill seeks to accomplish many of the same objectives of Senate Bill 2213. Like Senate Bill 2213, the bill authorizes states and private parties to sue telemarketers for fraudulent acts or practices. In addition, the bill requires the Commission to promulgate a telemarketing rule containing provisions similar to the Mail Order Rule enforced by the Commission. Furthermore, the bill prohibits telemarketers from harassing consumers.

By avoiding any reliance upon Section 19 of the Federal Trade Commission Act, the bill cures some of the deficiences inherent in Senate Bill 2213. States and private parties would not be precluded from seeking injunctive relief or be limited to prosecuting fraudulent practices that violate specific provisions of a rule to be promulgated by the Commission.

However, despite these efforts to eliminate the unintended consequences of an earlier draft of this bill, we continue to have the same reservations about the ultimate need for these provisions. In addition, this bill will not enhance significantly the ability of the Commission to fight against telemarketing fraud. For these reasons, we cannot recommend passage of House Bill 4101 as presently drafted.

SENATE BILL 2326

Of the three bills currently before the Subcommittee, we believe that Senate Bill 2326 has the greatest potential to make a significant impact on telemarketing fraud. Unlike the bills discussed earlier, the bill's primary focus is to arm the Commission with additional weapons specifically designed for fighting telemarketing fraud.

First, the bill would permit the Commission to bring Section 13 actions in one district against multiple defendants residing or transacting business in different districts. As noted earlier, we have experienced some difficulty in satisfying current venue requirements, which force us to establish that all defendants in a telemarketing lawsuit reside in or transact business in the same district in which the suit is brought. While Senate Bill 2213 also enables the Commission to sue multiple defendants in one district, it confines this authority to Section 19 actions. As discussed above, most of our telemarketing cases are brought under Section 13.

Second, the bill would amend the Right to Financial Privacy Act [22] to premit the Commission to delay notice to individuals when obtaining access to their financial records if there is reason to believe that such notice will result in the dissipation or removal of assets subject to redress or restitution. This provision, however, would still require the Commission to follow cumbersone procedures to obtain a court order granting delayed notice.[23]

Third, the bill would amend U.S. Postal Service Regulations to enable the Commission to use mail covers in the course of its investigations. Mail covers would allow us to make a record of any data appearing on the outside cover of any piece of mail sent by a suspect. This tool would be of great assistance to us in our telemarketing investigations because it would help us locate victims and potential witnesses. Ordinarily, finding victims who can testify to a fraudulent telemarketing sales pitch is difficult because victims often do not realize that they have been cheated until long after the fact.

Fourth, the bill would authorize the Commission to appoint state attorneys general to assist us in enforcing Commission promulgated rules. We suppot this provision because it encourages joint action with the states. In addition, unlike the other bills under consideration by the Subcommittee, this provision encourages a joint coordinated effort to stop telemarketing frauds rather than separates and possibly conflicting efforts by each of the fifty states and the Commission.

By coordinating our actions in this area with those of various state attorneys general, we have been able to develop a consistent, coherent approach to the enforcement of existing consumer fraud laws against various telemarketing scams. Moreover, Senate Bill 2326 encourages Commission attorneys and investigators to work side-by-side with state authorities in investigating and prosecuting telemarketing frauds. We have found this relationship to work well in the past. For example, in one case, state officials in an FTC proceeding helped serve banks and financial institutions within their jurisdiction with federal court orders freezing the assets of the defendants as part of a coordinated effort to preserve assets for future redress. In still another case, both the Commission and the Attorney General for the State of Minnesota filed simultaneous complaints against the same telemarketers. Since then, we have closely coordinated discovery and have sought to consolidate parallel aspects of the two proceedings.[24] We question whether Senate Bill 2213 and House Bill 4101 would be as effective in encouraging such cooperation in the future.

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[22] 12 U.S.C. 3401 *et seq.*

[23] This provision could provide the Commission with an even more valuable tool if the procedures were made less burdensome or if it exempted us, as it now exempts state authorities, from providing any notice to fraudulent operators of telemarketing scams.

Fifth, the bill would enable the Commission to require the production of physical evidence pursuant to civil investigative demands. Currently, Section 20 of the Federal Trade Commission Act only permits the Commission to require the production of documents or testimony. By allowing the Commission to compel the production of physical property, such as allegedly rare coins or works of art for expert examination or appraisal, the bill enhances our ability to investigate telemarketing scams.

Sixth, the bill would specify the manner in which the Commission could serve process in Section 13 actions. As presently drafted, the applicable provision in the bill may not provide us with additional enforcement tools in this area since the Commission already possesses these means of serving process under the Federal Rules of Civil Procedure.

Seventh, the bill would require the Commission to conduct a study of unfair and deceptive acts or practices in the life care home industry and, if warranted, initiate a trade regulation rule proceeding. We share the concern expressed by Senator McCain during the Commission's March hearing on issues affecting the elderly about the problems with both fraud and unintentional mismanagement in the life care industry. The Commission's reauthorization bill currently pending before Congress would enable us to conduct such a study. We are presently examining the extent to which jurisdictional limits on our ability to proceed against not-for-profit organizations could impede the ability of the Commission to respond to instances of fraud and deception in this area.

Finally, Senate Bill 2326 would require the Commission to amend the Mail Order Rule to apply to telemarketing. As noted above, we believe that the provisions contained in the Mail Order Rule are unlikely to address the practices that characterize the typical telemarketing fraud. In addition, the Commission may require more than the 270 days allotted to it by this bill to amend the Mail Order Rule to comply with our rulemaking authority under the Magnuson-Moss Warranty—Federal Trade Commission Improvement Act, 15 U.S.C. 2301. As an alternative, we suggest that the bill authorize the Commission to promulgate the rule under Section 553 of the Administrative Procedures Act, 5 U.S.C. 551, which would enable us to act more expeditiously.

CONCLUSION

In conclusion, we believe that, on balance, Senate Bill 2326 offers the greatest potential of the three bills to curb telemarketing fraud. Only Senate Bill 2326 significantly enhances our ability to protect consumers from telemarketing abuses. The bill eliminates one of our major jurisdictional limitations and gives us powerful additional tools with which to fight telemarketing fraud. In addition, the bill encourages the Commission and attorneys general of the states to work together to mount a cooperative attack on telemarketing fraud.

As intended, Senate Bill 2326 will make it easier for the Commission to bring civil actions against fraudulent telemarketers. We would like to stress, however, that we do not believe that an increased number of civil actions will rid the economy of this problem. States and other federal authorities with criminal jurisdiction should be encouraged to bring more criminal prosecutions and advocate stiff sentences and fines against telemarketing con artists. While there may always be a need for civil actions to ensure that perpertrators of fraud are required to return their ill-gotten gains, the additional threat of jail would be more likely to deter the most egregious fraud artists.

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[24] As a result of these efforts, we have had some success in joining the two cases under a theory of pendant party jurisdiction.

Senator GORE. Our next witness is Mr. Robert Stephan, Attorney General of the state of Kansas. General Stephan is representing the National Association of Attorneys General, and we are delighted that you could join us. Without objection your full statement will appear in the record, and we invite you to proceed with a summary as you see fit. Please proceed.

STATEMENT OF ROBERT STEPHAN, ATTORNEY GENERAL, STATE OF KANSAS

Mr. STEPHAN. Thank you, Senator Gore, Senator McCain.

I should note that Commissioner Calvani and I agree on one thing. I noticed in the last issue of Sigma Chi Magazine that he was a member of that fraternity, and I also, but I think it stops there.

I sat here and listened to testimony that S. 2313 would be a privatization of lawsuits, and I frankly am somewhat miffed by that. State Attorneys General do not file private actions. They file actions on behalf of their individual states in order to protect the citizens in those states. And in this particular instance and in regard to the two bills being discussed today, that action would involve telemarketing fraud.

And it seems to me that this is more a turf battle than anything else at this point, because both S. 2313 and S. 2336 allow an attorney general to be involved in federal court in regard to a telemarketing fraud action. The difference is that under S. 2313 you do not have to wait around forever for the FTC to designate someone to bring a case in federal court. Under S. 2313, a suit can be brought quickly by a state attorney general.

I should mention that approximately 150 telemarketing fraud cases have been filed by attorneys general in the various states of this country in the last 18 months. And so when the Commissioner mentioned that there was a difference of opinion on what was telemarketing fraud since they filed only 27 over a period of several years, I would certainly concur in that statement.

I think it is important that attorneys general be involved, and let me say that in many instances, the attorneys general have received a great deal of cooperation from the Federal Trade Commission in this area, but certainly there are differences of opinion in regard to how we should proceed. But more importantly than that, personal beliefs really do not have any place in this area. I think it is logical to conclude that an individual consumer in a state is not going to call a member of the Federal Trade Commission to complain about some fraudulent activity that has occurred on the telephone. They are not even going to call their United States Senator. They are going to call the Attorney General's office——

Senator MCCAIN. You are wrong. They do call their United States Senator all the time.

Mr. STEPHAN. ——about consumer fraud.

Senator McCAIN. Absolutely.

Mr. STEPHAN. Well, they call the FTC too, Senator, and they filed 27 cases over a period of years.

Senator McCAIN. I do not know about that, but I know your statement is wrong when you say they do not call their Senators.

Mr. STEPHAN. Well, I could get into a debate with Commissioner Calvani as to what action he takes, but I do not think I should do that with you.

Let me just state that time is of the essence, and it is important, and we do get immediate notice of some kind of fraudulent activity, and it varies, and you can hear one more story after another as to the boiler room techniques. One is the speedboat that was sold over the telephone, and people got it and it was a rubber raft with an engine that would not beat an egg. In fact, we bought one, and I can say intentionally so to see what it was like, and we put it in a swimming pool and we had to push it to make it go.

On one telemarketing deal a call was received by consumers, and they were told they could get vitamins for 395. They thought it was $3.95, but it was $395. That goes on and on and on.

An attorney general can simply take action more quickly than a federal agency, and that is not to criticize any federal agency. It is just the closer you are to the people who have been harmed, the more quickly you can respond. And so that is why I am not here to criticize the Federal Trade Commission, but just to say that the attorneys general of this country are responsible. Obviously, you from your bills believe that they are because both bills allow participation by the various state attorneys general.

I am most appreciative of the opportunity to appear here on behalf of the National Association. As a former president of the National Association of Attorneys General, I know that this is a very serious problem and is of great concern to the attorneys general of this nation, and I am pleased to voice support for S. 2313 and certainly to voice support for the intent of involving attorneys general that is in S. 2336.

Senator GORE. Thank you.

We had an exchange earlier with Commissioner Calvani about the joint NAAG-FTC data base. How many states participate in this?

Mr. STEPHAN. There are approximately 17 states presently involved in that data base and if I might just extend that somewhat, there are six or seven that we expect to come on line fairly shortly. It was an experimental program. Funding is always a problem, and that is why it has moved rather slowly.

Senator GORE. I see. And that is why all 50 do not participate?

Mr. STEPHAN. In the main it is a matter of finances. The other is, we wanted to see how it might work out.

Senator GORE. Is it working pretty well or not?

Mr. STEPHAN. It is my understanding that it is working well, yes, sir.

Senator GORE. Now, some people have expressed the fear that a grant of authority to the state attorneys general would create a situation where the attorneys general run wild in this area, to use the phrase some have used, pursuing legitimate telemarketers who then would have to expend much time and effort defending themselves against those suits. How would you respond to that concern? I am sure you have heard it expressed also.

Mr. STEPHAN. Many times. In fact, I am sure that anytime anyone in public office tries to take some type of action, they are always accused of either being political or of picking on people.

I am very proud of the attorneys general of this country. I think they act responsibly. I think if they have an opportunity to bring a telemarketing fraud case in federal court, they will not be interested in going after legitimate businesses. They are interested in going after those who have fraudulently tried to deceive consumers.

Senator GORE. Why do you prefer the approach in the Gore-Luken bills rather than the deputization approach used in the McCain bill?

Mr. STEPHAN. It is mainly the time aspect that is involved, Senator Gore. When you have to be deputized, it takes time to get that done. Telemarketing fraud people try to wrap up their business as quickly as possible and fold up and disappear. And the more quickly you can act, the more of a chance you have to stop the fraud and to obtain funds for those who have been defrauded.

Senator GORE. Would you have any concern that this administration might be reluctant to use the deputization procedure?

Mr. STEPHAN. Well, I do not know whether they would be reluctant to use it or not since the testimony from the Federal Trade Commission is that they do not want attorneys general involved in what they call private lawsuits. I would think that there might be some reason to believe that they do not want us involved at all.

Senator GORE. Are you aware of instances where the FTC and the attorneys general have begun actions against telemarketers with the attorney general proceeding under state law and the FTC under the FTC Act and then attempting to coordinate the dual actions?

Mr. STEPHAN. I cannot cite any specific cases. There have been instances certainly when there has been cooperation between the Federal Trade Commission and various attorneys general.

Senator GORE. Our records indicate that there may have been a case in Minnesota where coordinated discovery efforts have been conducted, and if your association wishes to expand on that for the record, we would appreciate it.

Mr. STEPHAN. All right.

Senator GORE. Now, you testified that a unified national effort is needed to curtail unfair and deceptive practices. If this bill were to become law, the bill that passed the House, that is, could you anticipate or would you anticipate some coordination among the attorneys general to ensure that duplicative actions are not begun?

Mr. STEPHAN. Well, of course, we have an office that houses a staff for the National Association of Attorneys General. If the bill were passed and an attorney general filed a telemarketing fraud case, other attorneys general could be instantly notified and could join in that action.

Senator GORE. What about the authority to go to court for fraudulent acts or practices? Is that term "fraudulent" well defined in the law or is it subject to varying interpretations?

Mr. STEPHAN. I do not think there is a great deal of variance in the interpretation. I think that when these boiler room operations get under way and people in your particular state have been taken advantage of, it does not take any genius to figure out that they have been hooked and crooked.

Senator GORE. Two of your 50 members, the attorneys general of New Mexico and Utah, have submitted testimony expressing concerns about giving independent authority to the state attorneys general. Do you have any reaction to those statements?

Mr. STEPHAN. Well, they are both fine individuals. I disagree with them and evidently 48 other attorneys general disagree with them.

Senator GORE. The Congressional Budget Office says that the aggregate number of cases nationwide could go down if H.R. 4101 and S. 2213 were enacted. Do you agree and do you believe this might result in lower administrative and court costs for state governments?

Mr. STEPHAN. I do not know what the fiscal impact would be in regard to the bill itself, Senator.

Senator GORE. All right, if you wish to elaborate for the record, you are free to do so.

Mr. STEPHAN. Thank you.

Senator GORE. H.R. 4101 and S. 2213 permit actions to be brought by state attorneys general and other state officials who are vested with the authority to enforce state consumer protection laws. Who are these other officials and how many are there? Might their actions duplicate the efforts of state attorneys general?

Mr. STEPHAN. Sometimes in some states you have the office of the district attorney who has certain consumer protection powers, but the bill limits action by an attorney general, as I understand it. And so a district attorney's office would not be authorized to go to federal court unless the attorney general of that state was involved.

Senator GORE. All right, very good. I will have additional questions in writing, but I will now recognize Senator McCain.

Senator MCCAIN. Thank you, Mr. Chairman. First of all, thank you for your very fine testimony, Attorney General Stephan. We appreciate it very much.

It seemed to me that privatization seemed to be a matter of concern to you since you mentioned it three or four times in Mr. Calvani's testimony. My understanding of his testimony when he was talking about privatization had nothing to do with you, sir. It had to do with the ability of private citizens to bring suit and the concern he had about the abuses of RICO, which are being addressed in the judiciary committees of both houses right now.

Mr. Chairman, before we go much further, I would like to have introduced as part of the record the statement of the Attorneys General of the states of New Mexico and Utah, and I know of at least one other state that supports their statement.

Did you take a vote on that resolution at your meeting?

Mr. STEPHAN. We did.

Senator MCCAIN. You did have a vote.

Mr. STEPHAN. We did. And also under our procedures, Senator, even if an attorney general is not present, that attorney general may register a dissent.

Senator MCCAIN. What was the vote?

Mr. STEPHAN. I do not recall how many attorneys general were present generally. Certainly over 30. And the only two who registered a dissent to my knowledge were the attorneys general of Utah and New Mexico.

Senator MCCAIN. But all 50 states were not polled, is that correct?

Mr. STEPHAN. No. I would say not all 50 states are polled, that is correct.

Senator GORE. But all have an opportunity or are advised of the action and have an opportunity to express their opinions?

Mr. STEPHAN. Absolutely, and that is made a part of the record.

Senator MCCAIN. How many resolutions did you discuss during that meeting?

Mr. STEPHAN. I do not remember how many resolutions.

Senator MCCAIN. Quite a few?

Mr. STEPHAN. Well, really not very many.

Senator MCCAIN. I was told that—well, your assistant seems to be very animated behind you. Perhaps she would want to tell us.

Mr. STEPHAN. You are right, she is animated, and she said approximately 10.

Senator MCCAIN. Thank you, Mr. Attorney General. I appreciate it. It seems to me that criminal sanctions would be effective against telemarketing fraud. You said you did not agree with Commissioner Calvani on anything, so I take it that you did not agree with him on that, is that correct?

Mr. STEPHAN. Well, I have to tell you that I just wonder what good it does to throw up new criminal laws all the time when no one goes to jail. Certainly there are some criminal statutes that take care of theft of property and so forth. I am certainly not opposed to it, but I do not think it is a catchall and a cure-all by any means at all.

Senator MCCAIN. I am not sure I understand your statement about criminal statutes where no one goes to jail. I am not sure I understand that.

Mr. STEPHAN. Well, I would say that the odds on anyone going to jail in the federal courts as a result of being convicted of telemarketing fraud are very slim, and people who are involved in the criminal business know that.

Senator MCCAIN. On what experience do you base that statement?

Mr. STEPHAN. By watching the courts year after year after year.

Senator MCCAIN. Do you know of many cases where criminal action has been brought on telemarketing fraud before the federal court?

Mr. STEPHAN. I do not, but I know of nonviolent offenses that are brought before the court, and it is not likely that nonviolent offenders are incarcerated in penal institutions other than income tax evaders.

Senator MCCAIN. Generally my understanding that it is the state law enforcement people that bring criminal suits. How many criminal actions has your state brought in such cases?

Mr. STEPHAN. In regard to telemarketing fraud?

Senator MCCAIN. Yes.

Mr. STEPHAN. I can only recall one.

Senator GORE. If the gentleman would yield briefly, how many civil cases?

Mr. STEPHAN. We have had a number of civil cases. I do not have the numbers but, as I said, the state attorneys general as a whole have brought 150 or so cases in the last 18 months. And many times we are able to resolve some of these issues without suit or suit is just of no avail because you just cannot find them.

Senator MCCAIN. What percentage of your state's budget is allocated for educating consumers about telemarketing fraud? Do you happen to know that?

Mr. STEPHAN. I do not know from a percentage standpoint.

Senator MCCAIN. Is it substantial, do you think?

Mr. STEPHAN. No, it is not substantial. Of course, I doubt if Kansans need as much education as some, and that may be part of it in my particular state.

Senator MCCAIN. They are certainly a very highly intelligent group of citizens, sir, because they come to Arizona for the winter.

May I ask just one more question, and I do appreciate very much your testimony, and I appreciate the job that you have done on behalf of the people of the state of Kansas.

What enforcement options are currently available to you in addressing this issue?

Mr. STEPHAN. Generally just the filing of suit in the state court. There just really are not many other options available.

Senator MCCAIN. Thank you.

Thank you very much, Mr. Chairman.

Mr. STEPHAN. Thank you very much, sir.

Senator GORE. Thank you very much, General Stephan. We will have extra questions in writing, if you do not mind responding.

Now, I would like to call up all of the witnesses on our first panel. They are Mr. Dennis Brosan, Director of security for Visa USA; Ms. Joan Mullen, President of the Telemarketing Division of Zacson Corporation; Paul Williams, President of the National Office Machine Dealers Association; and Michael Altier, Vice President and Legislative Counsel for the National Retail Merchants Association.

If all of you would join us at the witness table, we would appreciate it. Without objection we are going to put your entire prepared statements into the record and because of time constraints, we are going to use this lighting system and ask you to limit your prepared remarks to five minutes, and the lights will give you an indication of when that time has expired, and we would appreciate your cooperation. We will begin with Mr. Dennis Brosan with the Visa USA company, headquartered in McLean, Virginia, and you are Director of Security there. We are most glad you could be here. Please proceed.

STATEMENT OF DENNIS BROSAN, DIRECTOR OF SECURITY, VISA USA

Mr. BROSAN. Thank you, Mr. Chairman, and members of the committee, and I appear not only for Visa, but I also appear on behalf of MasterCard International. The subcommittee is to be commended for considering federal legislation to address the important issue of telemarketing fraud.

Senator GORE. If you could bend the neck of your microphone down a little bit, it would pick up your voice a little bit better, and we could hear. Thank you.

Mr. BROSAN. As we have heard, the FTC estimates that losses due to telemarketing fraud exceed $1 billion per year. Financial institutions suffer substantial losses from telemarketing fraud when a consumer cancels a credit card transaction for which the financial institution has already made payment to the fraudulent telemarketing operator. MasterCard and Visa estimate that financial institutions lose in excess of $100 million per year as a result of these telemarketing fraud schemes.

The losses do not, of course, include those instances where consumers decide not to contact their banks about a fraud loss because, for example, they are embarrassed at having been taken or in instances where the payment is not a credit card. Visa and MasterCard and their members have been aggressive in their efforts to address telemarketing fraud. For example, MasterCard and Visa have actively cooperated with law enforcement agencies to prosecute telemarketing fraud operators. They have taken steps to educate their member financial institutions and the consumers about fraudulent telemarketing practices and have developed procedures to preclude the fraudulent telemarketing operators from the credit card systems.

Despite these extensive efforts, sophisticated fraudulent telemarketers continue to gain access to the credit card system. For example, some fraudulent telemarketers establish business relationships which they operate in a legitimate fashion for some time in order to gain the confidence of the bank providing the credit card payment services. They then begin their fraudulent activity at a later date.

Other fraudulent telemarketers have successfully persuaded merchants with Visa or MasterCard contracts to submit the telemarketer's sales drafts into the credit card system in the name of that merchant. This practice violates MasterCard and Visa rules, and it is called factoring.

Telemarketing fraud losses will continue to mount without an effective federal legislative response to this national problem. State and local enforcement agencies often with the assistance of Visa and MasterCard or their member institutions have initiated actions against fraudulent telemarketers only to be frustrated by state law jurisdictional limits. These jurisdictional limits make it difficult to prosecute or obtain relief from fraudulent telemarketers who locate their operations outside the states in which their victims reside or who move frequently to avoid detection and prosecution under state law.

In addition, fraudulent telemarketing schemes are too numerous and too widespread to be controlled by federal agencies alone. We believe that S. 2213, the Telemarketing Fraud Prevention Act of 1988, will provide an effective federal response to the problem of telemarketing fraud. S. 2213, unlike S. 2326, provides a private right of actions which consumers, financial institutions and other victims of telemarketing fraud may bring against the telemarketers.

MasterCard and Visa believe that the private right of action contained in S. 2213 is an essential element of effective federal response to telemarketing fraud. Such private right of action would permit those are in the best position to first detect the telemarketing fraud, the victims, to act quickly to stop fraudulent operations when they are discovered because S. 2213 would permit such actions to be brought in federal court, victims could obtain appropriate relief regardless of where in the United States the fraudulent operators are located or have moved to. As a result, financial institutions and other victims who currently are hampered by the limitations of the existing statutory scheme could utilize their own resources to assist in the fight against telemarketing fraud.

Visa and MasterCard recognize, however, that any new remedies to address telemarketing fraud must contain appropriate safeguards to ensure that legitimate merchants are not inappropriately affected. For example, the House of Representatives passed H.R. 4101 which is the companion legislation to S. 2213. H.R. 4101 requires that a plaintiff must suffer $10,000 in damages to bring a private cause of action. MasterCard and Visa support this $10,000 threshold which is generally consistent with federal jurisdictional requirements and would ensure that the federal courts are reserved only for the most significant cases.

Indeed Visa and MasterCard would like to take this opportunity to suggest an amendment to the private cause of action provided in S. 2213 to further safeguard against frivolous suits. MasterCard and Visa recommend that S. 2213 be amended to provide the federal courts with exclusive jurisdiction over all private causes of action brought under 2213. This amendment would ensure that the existing safeguards applicable to federal court litigation but not necessarily to state court litigation would apply to all private causes of action brought under S. 2213.

Visa and MasterCard also believe that state attorneys general should play an important part in the fight against telemarketing fraud as would be provided under both 2213 and 2326. In the past MasterCard and Visa have worked closely with several state attorneys general and have found them to be helpful in pursuing fraudulent telemarketers.

Finally, Visa and MasterCard believe it is imperative that effective legislation be enacted during the session of Congress. According to FTC estimates, losses from telemarketing fraud are amounting at a rate of

$2.4 million per day. Holding this legislation over until the next session of Congress will result in millions of dollars of telemarketing fraud losses which should otherwise have been avoided by prompt Congressional action during this session.

That concludes my prepared remarks. I will be happy to answer questions.

[The statement follows:]

STATEMENT OF VISA U.S.A. INC. AND MASTERCARD INTERNATIONAL, INC.

MasterCard International, Inc. ("MasterCard") [1] and VISA U.S.A. Inc. ("VISA") [2] appreciate the opportunity to testify before the Consumer Subcommittee of the Committee on Commerce, Science and Transportation of the U.S. Senate ("Subcommittee") on the important issue of telemarketing fraud legislation. The Subcommittee is to be commended for considering federal legislation to address the problem of telemarketing fraud. For the reasons discussed in this testimony, VISA and MasterCard urge the Subcommittee to proceed to mark up this legislation as quickly as possible so that the legislation can be enacted during this session of Congress.

The FTC estimates that losses due to telemarketing fraud exceed $1 billion per year. These losses most frequently result from fraudulent telemarketers who solicit consumers by telephone and dupe them into purchasing goods or services which are substantially inferior to those which have been promised or which the fraudulent telemarketers have no intention of delivering. Our statement will focus primarily on telemarketing fraud involving credit cards.

The earliest telemarketing schemes involved the solicitation of a consumer over the telephone, during which time the fraudulent operator obtained the consumer's credit card number. The fraudulent operator subsequently charged the consumer for products that were substantially inferior to those the consumer expected based on representations made during the telephone solicitation or submitted unauthorized charges utilizing the consumer.s credit card number. The victimized cardholder generally became aware of the telemarketing scheme upon reviewing his or her credit card statement or upon inspecting the products received. Thus, these early telemarketing schemes typically had a relatively short life span because the scheme would come to light during the first or second credit card billing cycle after the cardholder was victimized or upon receipt of the inferior products.

The telemarketing schemes perpetrated today, however, are significantly more sophisticated. Current telemarketing schemes typically involve significant time delays between the time at which charges are incurred on the credit card and the delivery of the promised good or service. As a result, such schemes are extremely difficult to detect at their inception and many consumers fail to realize they have been duped until a substantial period of time has gone by and the fraud is uncovered. For example, under travel scam programs, the consumer generally is charged for the "bargain" travel package shortly after providing his or her credit card number to the fraudulent operator, but typically the consumer does not attempt to take the trip until several months later. Since a significant amount of time normally elapses between the time charges are incurred and the time the telemarketer is required to deliver goods or services, the fraudulent operator is able to continue this type of scheme in its existing form for a significant period of time.

Travel scams constitute the great majority of telemarketing fraud. Nevertheless, other types of telemarketing fraud also have been experienced in recent years. For example, consumers promised cameras, mink coats, television sets and other "prizes" have been convinced to purchase vitamins at greatly inflated prices only to find that their prizes do not exist or are worth far less than expected. Other consumers were offered gold bullion at discount prices but were told that orders had to be placed two or three months in advance. The gold was never delivered.

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[1] MasterCard is a membership organization comprised of financial institutions that are licensed to use the MasterCard service marks in connection with payment systems, including credit cards.

[2] VISA is a membership association comprised of financial institutions in the United States that are licensed to use the VISA service marks in connection with payment systems, including credit cards.

One fraudulent operator established an actual credit card registration service and promised cardholders that the service would notify appropriate financial institutions in the event that the cardholder's credit cards were lost or stolen. Although the service apparently conducted legitimate credit card registration activities, it also defrauded consumers. Consumers were told they could use the service without charge for six months but were in fact charged for the service immediately upon registration.

Because credit cards frequently are used as the method of payment in telemarketing transactions, financial institutions suffer substantial losses when consumers cancel transactions upon which payment to the telemarketing merchant perpetrating the fraud has already been made by a financial institution and the financial institution cannot locate or otherwise obtain reimbursement from that fraud operator. MasterCard and VISA estimate that financial institutions lose in excess of $100 million per year as a result of these telemarketing fraud schemes. These losses do not include instances where consumers decide not to contact their banks about a fraud loss for a variety of reasons, including embarrassment at having been "taken," or where consumers use a payment mechanism other than a credit card.

Many of the telemarketing frauds uncovered during the past few years have involved losses in excess of $1 million each. In fact, two banks recently have reported telemarketing fraud-related losses for a one-year period in excess of $2.5 million. In addition, financial institutions spend millions of dollars each year to review and investigate individual cardholder complaints, process adjustments to cardholder accounts, pursue and prosecute particular telemarketing fraud operations, and combat telemarketing fraud generally.

Moreover, beyond out-of-pocket costs, telemarketing fraud poses a threat to the very integrity of the credit card systems themselves. The benefits currently enjoyed by consumers, businesses and other participants in this country's credit card system result, in part, from the widespread acceptability of credit cards as a medium of payment. This acceptability is related directly to the reliability of the systems and the confidence placed in them. Telemarketing fraud threatens to undermine this confidence.

VISA and MasterCard and their members have been aggressive in their efforts to address telemarketing fraud. For example, MasterCard and VISA have actively cooperated with federal and state law enforcement agencies and other federal and state agencies to address telemarketing fraud, and will continue to do so. As a result of these coordinated efforts, several cases have been successfully prosecuted in recent years.

VISA and MasterCard also are educating their member financial institutions and consumers about fraudulent telemarketing practices. For example, MasterCard and VISA have sent several formal communications to their member financial institutions concerning the problem of telemarketing fraud and have prepared a "statement stuffer" for members to distribute to cardholders warning of the dangers posed by telemarketing fraud. VISA and MasterCard also have prepared a crime prevention advertisement and videotape concerning telemarketing fraud.

In addition, MasterCard and VISA have established procedures to identify businesses engaged in fraudulent practices, including telemarketing fraud, and to deny them access to the credit card payment systems. In this regard, VISA and MasterCard require member financial institutions to investigate merchants applying for entry into the MasterCard and VISA payment systems. Pursuant to these merchant investigation requirements, several procedures must be performed by VISA and MasterCard member institutions before a merchant can be licensed to accept MasterCard or VISA credit cards. At a minimum, before accepting a merchant, a member institution must conduct: (1) a credit check and/or other financial background investigation; (2) a physical inspection of the merchant's place of business; and (3) a check to determine if the merchant has been previously terminated for fraud or suspected fraud.

Though seemingly simple, these screening procedures must be implemented very carefully in order to protect the legitimate interests of honest merchants. As a result, member institutions are required to engage in a delicate balance: on one hand the member institution must attempt to protect the integrity of the credit card system by denying access to dishonest merchants, while on the other hand the member institution must be cautious so as not to exclude or unduly hinder the activities of legitimate businesses that often rely heavily on the credit card payment systems. This balancing process is particularly difficult when the applicant is a new business with no performance record by which its trustworthiness can be judged. Despite these concerns, VISA and MasterCard believe this balancing effort is essential as credit card transactions comprise such a significant element of contemporary commerce.

MasterCard and VISA also assist member financial institutions in identifying businesses that accept credit cards for fraudulent or deceptive purposes. As a result of these on-going efforts, entities suspected of defrauding cardholders through telemarketing schemes have lost their access to the credit card systems. In addition, VISA and MasterCard have implemented procedures to track fraudulent telemarketing operators and prevent them from participating in the MasterCard or VISA systems through other member institutions.

Despite these extensive efforts of VISA, MasterCard and their members, sophisticated fraudulent telemarketers continue to gain access to the credit card systems. For example, fraudulent telemarketers have established seemingly legitimate businesses, and have operated these businesses in a legitimate fashion for some time in order to gain the confidence of a bank providing credit card payment services, prior to engaging in large-scale telemarketing fraud.

Other fraudulent telemarketers have successfully persuaded merchants with MasterCard and/or VISA contracts to submit the telemarketers, sales drafts into the credit card payment system in the name of that merchant. This practice, which violates VISA and MasterCard rules, is called "factoring." In the case of factoring schemes, the fraudulent telemarketers typically have fled the jurisdiction by the time the fraud is discovered and the merchants through which the credit card charges are submitted often are deluged with credit card chargebacks. (Certain of the sophisticated operators now factor sales drafts through several merchants at once to avoid detection.) Indeed, in one recent situation, the chargebacks associated with such a factoring scheme resulted in significant losses to the merchant and the bank involved and may have resulted in the bankruptcy of the merchant.

Telemarketing fraud losses will continue to mount without an effective federal legislative response to this national problem. State and local enforcement agencies, often with the assistance of MasterCard, VISA, or their member institutions, have initiated actions against fraudulent telemarketers, only to be frustrated by state law jurisdictional limits. These jurisdictional limits make it difficult to prosecute or obtain relief from fraudulent telemarketers who locate their operations outside the states in which their victims are located or move frequently to avoid detection and prosecution under state law. In addition, fraudulent telemarketing schemes are too numerous and too widespread to be controlled by federal agencies alone, given their priorities and resources.

We believe that the Telemarketing Fraud Prevention Act of 1988 ("S. 2213") will provide an effective federal response to the problem of telemarketing fraud. S. 2213 would require the FTC to promulgate rules concerning telemarketing fraud and would provide a private right of action which consumers, financial institutions and other victims of telemarketing fraud may bring against fraudulent telemarketers. In addition, S. 2213 would permit state attorneys general to sue fraudulent telemarketers in federal court.

The Consumer Fraud Prevention Act ("S. 2326") also contains provisions that would address telemarketing fraud. S. 2326 would require the FTC to promulgate rules concerning telemarketing fraud and would authorize the FTC to appoint state attorneys general to assist the FTC in enforcing its telemarketing rules. However, S. 2326 would not create a private right of action.

VISA and MasterCard believe that the private right of action contained in S. 2213 is an essential element of any effective federal response to telemarketing fraud. Such a private right of action would permit those who are in the best position to first detect telemarketing fraud—the victims—to act quickly to stop fraudulent operations as soon as they are discovered. Because S. 2213 would permit such aCtions to be brought in federal court, victims could obtain appropriate relief regardless of where in the United States the fraudulent operators are located or have moved. As a result, financial institutions and other victims who currently are hampered by the limitations of the existing statutory scheme could utilize their own resources to assist in the fight against telemarketing fraud.

MasterCard and VISA recognize, however, that any new remedies to address telemarketing fraud must contain appropriate safeguards to ensure that legitimate telemarketers and other legitimate merchants are not inappropriately affected. For example, H.R. 4101, which is the companion legislation to S. 2213 passed by the House of Representatives, requires that a plaintiff must suffer $10,000 in damages to bring a private cause of action under H.R. 4101 against a fraudulent telemarketer. VISA and MasterCard support this $10,000 jurisdictional threshold, which is consistent with federal jurisdictional requirements generally and would ensure that the federal courts are reserved for only the most significant cases.

Indeed, MasterCard and VISA would like to take this opportunity to suggest a further amendment to the private cause of action provided in S. 2213 to further safeguard against frivolous suits. VISA and MasterCard recommend that S. 2213 be amended to provide the federal courts with exclusive jurisdiction over all private causes of action brought under S. 2213. Such an amendment would ensure that the existing safeguards applicable to federal court litigation, but not necessarily to state court litigation, would apply to all private causes of action brought under S. 2213 and would encourage consistent interpretation and application of S. 2213 throughout the nation.

MasterCard and VISA also believe that the state attorneys general should play an important part in the fight against telemarketing fraud. In the past, VISA and MasterCard have worked closely with several state attorneys general and have found them to be helpful in pursuing fraudulent telemarketers. Thus, MasterCard and VISA believe that federal legislation to address telemarketing fraud should provide a role for state attorneys general so that they, unimpeded by the jurisdictional limitations of state law, may assist federal law enforcement agencies as would be provided under both S. 2213 and S. 2326.

Finally, VISA and MasterCard believe it is imperative that effective federal legislation be enacted during this session of Congress. According to FTC estimates, losses from telemarketing fraud are mounting at a rate of $2.4 million per day. Holding this legislation over until the next session of Congress will result in millions of dollars of telemarketing fraud losses which otherwise could have been avoided by prompt Congressional action during this session.

Senator Gore. Thank you. We will hold off on our questions until the whole panel has finished.

I would like to call next on Joan Mullen, President of the Telemarketing Division of Zacson Corporation, appearing on behalf of the American Telemarketing Association. Please proceed, Ms. Mullen.

STATEMENT OF JOAN MULLEN, PRESIDENT, TELEMARKETING DIVISION, ZACSON CORP., ON BEHALF OF THE AMERICAN TELEMARKETING ASSOCIATION

Ms. Mullen. Mr. Chairman and members of the committee, my name is Joan Mullen, and I am the Chairman of the National Legislative Committee of the American Telemarketing Association.

Senator Gore. Excuse me, if you could move that microphone a little bit closer to you. Thank you.

Ms. Mullen. I appreciate the opportunity of appearing before you today on behalf of the ATA to discuss our activities to combat telemarketing fraud and our interest in the legislation on this subject pending before this committee.

I have been involved with the telemarketing profession since 1971. I am currently the president of the Telemarketing Division of Zacson Corporation, which is headquartered in Pleasanton, California. We are a telemarketing service agency, and we have been in business for nine years representing our clients by telephone in various areas including sales, lead generation, public relations and marketing research.

The ATA is a national, not-for-profit trade association. We represent over 800 professional and telemarketing companies in an industry that employs between two and three million Americans across the country who use the telephone as a medium for conducting their business. Our association includes eight regional chapters. Northern California, Southern California, Illinois, Minnesota, Texas, Georgia, New England and Mid-Atlantic.

Telemarketing is one of the fastest growing segments of American business offering career opportunities to a wide range of people including the elderly, the disabled and others with special needs. We are an unusual profession because we can truly offer equal opportunities to succeed to a very diverse work group. It is projected that the size of our profession will increase to over eight million employees in the 1990's.

Telemarketing fraud not only makes victims of the public, it also victimizes legitimate telemarketers who are negatively affected by abuses. Most businesses that use telemarketing do so in a conscientious and professional manner. The significance of ethical standards is clearly understood and the necessity of professionalism is critical to success in this competitive environment.

Although press coverage frequently indicates otherwise, only a small percentage of businesses engage in fraudulent activity over the telephone. As in all other cases of business fraud, there is a great deal of sensationalism. Nevertheless, it is devastating to all concerned, to the duped and cheated consumers and businesses as well as to the legitimate telemarketers who must combat the negative effects.

The ATA shares your concerns regarding telemarketing fraud, and we agree in spirit with S. 2213 and S. 2326, as well as H.R. 4101. We would like to ensure, however, that the proposed legislation target the offenders without punishing those of us who operate our businesses at the highest ethical levels. The ATA stands ready to work with the Federal Trade Commission toward the establishment of a clearinghouse for handling telemarketing inquiries and the development of enforcement procedures. Our members subscribe to the ATA's telemarketing standards and ethics guidelines. The ATA has also published consumer guidelines, a brochure available to the public. This document provides an easy to understand guide for consumers to follow when dealing with the telemarketing call. Copies of both of these documents have been included with our written testimony, and I request that they be included in the record of this hearing.

Senator GORE. Without objection, they will be included by reference.

Ms. MULLEN. Thank you. In addition to these publications through our education committee and in conjunction with the University of Texas at Arlington, we have developed a certification process for telemarketers and management. Also, we work closely with the National Consumer League, the National Association of Attorneys General, and other interested groups including various state legislators. At all levels of the ATA we continually work to educate and develop the professionalism of our industry through seminars and conventions, local chapter meetings, and user group meetings.

To repeat, while we do agree in spirit with the proposed legislation, we make the following recommendations with regard to enforcement. We agree that interstate fraud is difficult to police without interstate powers. However, the legislation as proposed would be unprecedented in the granting of authority to states. As written, Senate bill 2213 and House bill 4101 would allow the Federal Trade Commission and possibly two or more attorneys general to prosecute the same case at the same time. This would confuse rather than aid enforcement. The ATA recommends centralized enforcement through the Federal Trade Commission.

It is our recommendation that legislation make it clear that authority granted to the FTC and its rules should preempt state action where interstate commerce is involved. However, if the FTC fails to act or deputizes state attorney general to act as provided in Senator McCain's bill within an appropriate period of time, the legislation could provide that an attorney general of a state or other appropriate official may bring a civil suit to enforce the FTC's rules.

In summary, the ATA stands ready to work with all interested parties for the elimination of telemarketing fraud. It is in this spirit of cooperation that we offer the expertise of our membership to assist in the legislative process. Thank you.

Senator GORE. I want to compliment you or on your testimony and we will certainly take your suggestions under advisement.

Next Paul Williams, President of the National Office Machine Dealers Association. Mr. Williams, welcome, and please proceed.

STATEMENT OF PAUL WILLIAMS, PRESIDENT, NATIONAL OFFICE MACHINE DEALERS ASSOCIATION

Mr. WILLIAMS. Thank you, Mr. Chairman. My name is Paul Williams, President of the National Office Machine Dealers Association, a not-for-profit trade association, headquartered in Kansas City, Missouri. I am a volunteer participant in the association while serving as president of Office World, Incorporated, a business equipment and systems company with offices in Owensboro, Kentucky, and Evansville, Indiana. I have spent many years in our industry, 31 to be exact, on behalf of manufacturers and as an independent dealer of office products. I am proud to be a part of the most dynamic growth industry in the world, the business equipment systems industry.

I appreciate this opportunity to provide you with some observations about our problems with fraudulent telemarketing in our industry. NOMDA, which is the acronym for National Office Machine Dealers Association, is composed of over 6,500 members. All business equipment systems dealers in all 50 states and 10 foreign countries. Our members are primarily family-owned businesses, and we play a very important role in the overall economy of the United States. Typically it is an independent businessman following in the footsteps of his father and his grandfather before him. The typical dealer would probably have gross annual sales of $1,250,000 and would typically employ some 10 to 15 employees, some of these devoted to the sale of the product. The majority of them, however, are dedicated to the service and the customer satisfaction after those products are sold.

About 90 percent of these 6,500 sell typewriters, word processors. 65 percent sell photocopy machines. 26 percent sell facsimile equipment, the fastest growth item in our industry at this time.

The supplies industry for today's office products has become a multibillion dollar industry. It is a phenomenal growth, and it has attracted numerous unethical companies whose business it is to charge exorbitant amounts to unsuspecting receptionists, charities, churches, school districts or virtually any office using business equipment. I know from personal experience of customers of ours—one comes to mind—the misrepresentation that they are Office World, Incorporated—received an irate call from a parochial elementary school where the nun was saying that how dare I call her and say that I was taking her copier machine out because my company had called and said that she was not buying sufficient number of supplies.

Obviously this is misrepresentation. Some fraudulent telemarketer tarnishing the credit image of our company in the marketplace and frustrating this nun to the point that she was ready to stop doing business with me. Now, how many of those never call we never know, but we only know about those who take the time to call it where we have time to straighten the matter out.

It is not unusual in the copier industry that a manufacturer's carton of toner would be 12 bottles. A fraudulent telemarketer may say I have that same case for half the price, and their case would have only two bottles with probably no more than 10 percent of the yield that would be practical to the application of the copier.

They use the name and reputation of ethical dealers, have slick sales presentations, inferior products and as we have heard today from other sources which we can only echo have cost the public millions of dollars.

In a survey of office equipment users conducted by Dataquest, a division of Dun & Bradstreet in October of '86 it was revealed that over 80 percent of those responding end users had been contacted by fraudulent telemarketers. It is an increasing problem in the United States.

According to postal authorities, estimates of more than $350 million are lost to fraudulent telemarketers' office supplies. The Better Business Bureau estimates the cost to more than a billion dollars, and the Federal Trade Commission, as we know, concurs with these estimates.

NOMDA recognized these problems in the 1970's, began acting as a clearinghouse for complaints from across the country regarding telemarketing fraud. The association receives between 20 and 30 written documented complaints of telemarketing fraud every week in addition to even more telephone complaints.

The substance of the majority of the complaints fall into four categories: One, supplies with highly inflated prices; two, substandard product; three, unordered supplies; or, four, harassment over the telephone.

Fraudulent telemarketers' office supplies typically work in a boiler room type setting containing numerous phones in a small work area. They operate with an orchestrated script and are masters at implication, creating impression that they are the local legitimate dealer.

Oftentimes a prior company calls and inquires about the make and model of the copier or the product in the victim's office using the ploy that they are conducting a serial number check or some similar survey. No sales effort is made during the initial call. Once the victim's trust is established through misrepresentation, the standard pitch is that the price of toner went up and the customer was not notified. The seller, however, claims to have reserved a few cartons at the old price, and will send it to the customer. The old price is almost universally four or five times the actual retail price of any particular brand of copy toner. Once the invoice is received, the customer may notice additional charges made for shipping and identified charges and in most cases —and sometimes these are greater than the amount of the product, just the shipping and receiving charges. When it is received, it is typically inferior, questionable quality, or the quantity is less than represented as we mentioned.

The scam is often uncovered when the customer calls the local dealer that he has purchased his copier from to complain about the invoice or machine performance. These victims who realize the fraud after the product is received but not yet paid for are almost always forced to endure verbal abuse and harassment while attempting to return the nonconforming products.

Even with the phenomenal amount of complaints received by the National Office Machine Dealers Association on a daily basis, it is estimated that a small percentage of actual victims bother to submit complaints in writing.

NOMDA's role in the fight against the fraudulent telemarketer has been three-pronged: to educate the consumer, to assist the enforcement authorities in their ongoing investigations and prosecutions, and to support remedial legislation in the area. Once a written complaint of telemarketing fraud is received in our offices, the information is entered into our computer data base and the complaint is then forwarded to the appropriate enforcement authority in the end user state and the Federal Trade Commission.

Legislation is being proposed such as 2213 will take great strides toward the goal of eliminating telemarketing fraud. This legislation combined with continued efforts to educate consumers could effectively eliminate the problem of fraudulent telemarketing in the eighties. NOMDA believes that S. 2213 will be an effective tool to rid the public of a serious problem.

NOMDA also supports the goals outlined in 2326. It is essential that federal and state enforcement officials be afforded a tool to combat this fraud. NOMDA believes that the private party should have his right as well. The language of S. 2326 should eliminate the discretionary assistance of the state attorney general and authorize their use of this vital legislation. Further, the exclusion of activity subject to another federal statute is overly broad and should be limited so as not to provide a convenient escape. All telephone communications are, in fact, governed by other federal statutes.

NOMDA supports a federal law which can effectively address the fraudulent telemarketing problem on a national basis. Victims should not have access to redress solely on the basis of their geographic location.

The U.S. Senate should be congratulated on addressing a serious problem and taking immediate action.

At the time for questions, I would like to observe that our general counsel, Mr. Robert Goldberg, is in the room, and thank you very much, Senator Gore.

[The statement follows:]

STATEMENT OF PAUL WILLIAMS, PRESIDENT, NATIONAL OFFICE MACHINE DEALERS ASSOCIATION

Good afternoon. My name is Paul Williams, President of the National Office Machine Dealers Association, a not-for-profit trade association headquartered in Kansas City, Missouri. I am a volunteer participant in our Association, while serving as President of Office World, Inc., a business equipment and systems dealership with offices in Owensboro, Kentucky and Evansville, Indiana. I have spent many years in our industry both on behalf of manufacturers and as an independent dealer. I am proud to be part of the most dynamic growth industry in the world—the business equipment and systems industry.

I appreciate this opportunity to provide you with some observations about the problem of fraudulent telemarketing that is plaguing our industry. NOMDA is composed of over six thousand, five hundred independent business systems and equipment dealerships, the majority of which are family owned. Our members are located in all fifty states as well as ten foreign countries. These independent dealers work together in a common effort, educating each other in the latest management, marketing and technical procedures.

The small, independent business systems and equipment dealer plays a very important part in the overall economy of the Unites States. The majority of the over four hundred manufacturers of business equipment have seen the advantages of marketing through an educated network of independent dealers. These dealers have close relationships with large and small businesses, consumers and the general community in their respective market areas.

Our typical member is a small, independent businessman, continuing in the footsteps of his father and his grandfather before him. Average gross sales volume of our members is $1,250,000 per year. Our typical member employs from ten to fifteen people, with several devoted to the sales of the products. The majority of his employees, however, are dedicated to service and customer satisfaction for those products sold.

Our membership represents approximately seventy percent of those independent dealers who primarily market business systems and equipment. These businesses carry lines of product ranging from simple desk top calculators to sophisticated computers. Some dealers may carry a combination of product lines from different manufacturers, as well as supplies of furniture. However, our Association's major concern is business systems and equipment. Almost ninety percent of NOMDA members sell typewriters/word processors, over sixty-four percent sell photocopy machines, and twenty-six percent sell facsimile machines: the fastest growing segment of our industry.

Office automation has increased the ease of communication throughout the world. Computers, word processors, typewriters, facsimile machines, and copiers have become an integral part of each of our working days. This reliable equipment is designed to operate efficiently and easily upon demand. The only impediment to successful operation is an occasional mechanical failure or more likely, a lack of ribbon, paper, toner, or other essential supplies. The supplies industry for today's office products has become a multi-billion dollar industry. This phenomenal growth has attracted numerous unethical companies whose business is to charge exorbitant amounts to unsuspecting receptionists, charities, churches, school districts, or virtually any office using business equipment.

Supplies for business equipment and systems are sold in numerous ways. There is direct marketing, catalog sales, walk-in business, and telemarketing. Although telemarketing is an effective and recognized means to sell supplies, it is the area where fraudulent practices have been perpetrated upon unsuspecting end-users. Fraudulent telemarketers using the name and reputation of ethical dealers, slick sales presentations, and inferior product, have cost the public millions of dollars.

In a survey of users of office equipment conducted by Data Quest, Inc., a division of Dunn & Bradstreet, Inc., in October of 1986, it was revealed that over eighty percent of those responding end-users had been contacted by a fraudulent telemarketer. The problem of fraudulent telemarketing is increasing in the United States. Exhibit A presents a small sample of news articles presenting the problem. According to Postal Service estimates, more than $350,000,000 a year are lost to fraudulent telemarketers of office supplies. The Better Business Bureau estimates the cost at more than a billion dollars per year and the Federal Trade Commission concurs with that estimate.

NOMDA recognizing the problem in the 1970's, began acting as a clearing house for complaints from across the country regarding telemarketing fraud. The Association receives between twenty and thirty written, documented complaints of telemarketing fraud per week in addition to even more telephone complaints. The substance of the majority of the complaints falls into four categories: (1) supplies with highly inflated prices; (2) substandard product; (3) unordered supplies; and/or (4) harasment over the phone.

Fraudulent telemarketers of office supplies typically work in a boiler room type setting containing numerous phones and a small work area. They operate with an orchestrated script (see Exhibit B) and a phone book and are masters at implication, creating the impression they are the local legitimate dealer. Oftentimes a pirate company calls and inquires about the make and model of the copier in the victim's office using the ploy that they are conducting a serial number check or some similar survey. No sales effort is made during the initial call. On a later call, by virtue of detailed cross referencing, the seller knows everything about the victim's copier. Once the victim's trust is established through misrepresentation, a standard pitch is that the price of toner went up and the customer was not notified. The seller, however claims to have reserved a few cartons at the "old price" and will send it to the customer. The old price is almost universally four to five times the actual retail price of any particular brand of toner. Once an invoice is received, the customer may notice additional charges made for shipping and unidentified charges. The additional and unidentified charges have at times been more than the price billed for the product by an ethical dealer. When product is received, it is typically of an inferior or questionable quality, or the quantity is less than represented.

The scam is often uncovered when the customer calls the dealer that he purchased his copier from to complain about the invoice or machine performance. If the complaint is service oriented, the service technician will attempt to diagnose the problem not knowing the customer has been using inferior toner. Once the problem is uncovered, the customer is informed that the company he has been buying supplies from is not providing the correct product and that use of the wrong kind of toner or developer in a copier voids most service contracts sold by the dealer and warranties provided by the manufacturer. On top of the cost and embarassment of using the wrong toner, the customer discovers he has paid four to five times the actual retail value for the product.

Those victims who realize the fraud after the product is received but not yet paid for, are almost always forced to endure verbal abuse and harassment while attempting to return the non-conforming products. The abuses are from collectors and/or collection agencies employed by the vendors.

The effect that telemarketing fraud has on the legitimate dealer is staggering. The "Paper Pirates" and "Toner Phoners", as they are called, affect not only the dealer's bottom line by fraudulently selling millions of dollars of toner, they also affect the dealer's reputation in the community. By using local dealers' names under which to operate and their customer goodwill and satisfaction, fraudulent telemarketers deliver inferior supplies at outrageous prices for product and shipping.

Even with the phenomenal amount of complaints received by the National Office Machine Dealers Association on a daily basis, it is estimated that a small percentage of actual victims bother to submit complaints in writing.

NOMDA's role in the fight against the fraudulent telemarketer has been three-pronged:

(1) to educate the consumer;

(2) to assist enforcement authorities in their ongoing investigations and prosecutions; and

(3) to support remedial legislation in the area. Once a written complaint of telemarketing fraud is received in our offices, the information is entered into our computer database and the complaint is then forwarded to the appropriate enforcement authority in the end user's state and the Federal Trade Commission. Our database, established in June, 1986 is ever growing and constantly becoming a valuable source of information. Database information is available to enforcement authorities who wish to use it for enforcement and education purposes.

Although NOMDA sees its role in this fight as three-fold, its number one priority and foremost role as an industry leader is one of education. The consumer must oe alerted so that he or she does not fall victim to such telemarketing scams. NOMDA has been attempting to educate consumers, dealers and enforcement authorities alike from as early as 1978. Since that time, the Association has published several hundred articles, news releases and information packets for dealers and consumers.

In recent years, the Association has also captured the attention of Federal enforcement authorities by alerting them to the dangers and pervasiveness of such telemarketing scams. In the recent past, NOMDA has been invited to participate in panel discussions and official presentations on the subject of fraudulent telemarketing, in an effort to better educate enforcement authorities and consumers alike. This effort is ongoing but cannot succeed in eliminating fraudulent telemarketing.

In addition to assisting enforcement authorities and continuing to educate consumers and dealers, NOMDA is also interested in supporting remedial legislation aimed at stopping the fraudulent solicitation by telephone of office supplies. The State of California has enacted legislation aimed at curbing the problem through registration of companies engaged in telemarketing. The Bill further requires telephonic sellers who are subject to the regulations, to appoint the Secretary of State as their agent for service of process. Approximately eighty to ninety percent of boiler rooms operating nationwide, are located in California. About six hundred fifty telemarketing operations have now registered in California. Postal Inspector authorities estimate as many as one hundred thirty of them could be guilty of fraudulent office product sales. Although the California Legislation assists many agencies in their investigations of California based telephone soliciting operations, it has done little to curb the problem of fraudulent telemarketing. It is also not a law under which enforcement authorities from outside the State of California can proceed for any violation other than the alleged perpetrator's failure to register under the California law.

Some states have been successful in taking an active role in protecting their citizens under existing statutes. The North Carolina Attorney Generals office has obtained several injunctions against allegedly fraudulent telemarketing operations and for a time had virtually halted the flow of calls to North Carolina residents. Individual dealers have also brought successful legal actions to protect their name and goodwill. The telemarketers were not stopped, however, merely diverted to other states and the diversion was only temporary. Once North Carolina eased up on its prosecution, the telemarketers resumed calling its residents, only this time under new business names.

The deregulation of the telephone industry has assisted fraudulent telemarketers. Being extremely mobile, these companies can move from state to state to carry on their operations often leaving phone companies with staggering bills. Although there are state laws prohibiting the practices, there often is insufficient time to locate and prosecute the parties before they move on. NOMDA believes that federal regulation of telemarketers is essential due to the interstate aspects of the fraud being conducted. The Federal Trade Commission and Postal Inspectors have successfully attacked telemarketers but their limited resources and scope of the problem make the elimination of the problem impossible. The legislation being proposed, S.2213, will take great strides toward the goal of eliminating telemarketing fraud. This legislation, combined with continued efforts to educate consumers, could effectively eliminate the problem of fraudulent telemarketing in the 1980's. NOMDA believes that S.2213 will be an effective tool to rid the public of this serious problem.

NOMDA also supports the goals outlined in S.2326. It is essential that federal and state enforcement officials be afforded a tool to combat this fraud. NOMDA believes that private parties should have this right as well. The language of S.2326 should eliminate the discretionary assistance of State Attorney Generals and authorize their use of this vital legislation. Furthermore, the exclusion of activity, subject to another Federal Statute, is overly broad and should be limited so as not to provide a convenient escape. All telephone communications are in fact governed by other federal statutes.

The National Office Machine Dealers Association supports a federal law which can effectively address the fraudulent telemarketing problem on a national basis. victims should not have access to redress solely on the basis of their geographic location. The United State Senate should be congratulated on addressing this serious problem and taking immediate action.

Mr. Robert Goldberg, NOMDA General Counsel, and I would be pleased to answer any questions you may have.

Senator GORE. Thank you.

Our final witness on this panel is Mr. Michael Altier, Vice President and Legislative Counsel with the National Retail Merchants Association.

We are pleased to have you here.

Please go ahead.

STATEMENT OF MICHAEL J. ALTIER, VICE PRESIDENT AND LEGISLATIVE COUNSEL, NATIONAL RETAIL MERCHANTS ASSOCIATION

Mr. ALTIER. Thank you, Mr. Chairman.

As you indicated, I am Vice President and Legislative Counsel of the National Retail Merchants Association. I am here to testify in behalf of NRMA, the nation's largest trade association for the general merchandise retail industry.

I would also like to note that our statement is endorsed by the American Financial Services Association.

The retail industry wholeheartedly supports efforts to put fraudulent telemarketers out of business. Their scams hurt not only consumers but also legitimate telemarketers.

However, it is our view that the current legislation does not accomplish its well-intentioned objectives and, due to its overly broad provisions, it is likely to cause more problems for legitimate businesses than it will solve.

The problem appears to focus on the ability to catch telemarketers who commit fraud.

Legitimate telemarketers are not the problem. If we were to make a mistake, customers and State and Federal officials know where to find us.

This legislation, while perhaps helping to catch some fraudulent telemarketers, would impose substantial burdens on our members.

Let's face it: the people you really want to get at could care less about new statutes, rules and regulations.

Under the three bills that are pending before the subcommittee, telemarketing, which is defined to include virtually any aspect of our advertising or marketing, so long as it involves a phone call, goes far beyond what is ordinarily considered telemarketing.

The definition could cover all facets of catalogue, ordering by phone, many insurance transactions or stock brokerage activities, telephone dealings between suppliers and vendors, auto shop repairs, airline reservations and ticketing, real estate brokerage, and all other business activities that ordinarily or incidentally involve a telephone offer or sale.

According to the House report to H.R. 4101, the only limitation on this extremely broad definition is the "occasional use of a telephone by a person to sell, for example, his or her house or car."

Under the proposed legislation, legitimate telemarketers would be subject to Federal lawsuits by State attorneys general, other State officials and private parties, including competitors. This is a prescription for chaos.

It will create a proliferation of inconsistent enforcement activities and differing legal interpretations, which will result in a legal nightmare for retailers, especially those who operate in a multi-state environment.

The proponents of this legislation claim it will promote consistency. It will do just the reverse. Instead of being subject to the possibility of two levels of enforcement, that is, lawsuits brought by State attorneys general at the State level and by Federal authorities nationwide, as is the case under current law, H.R. 4101 would also subject legitimate retailers to Federal lawsuits brought by State attorneys general for their own and other States, as well as private party initiated actions in Federal court.

In short, H.R. 4101 creates many avenues for inconsistent enforcement policy, not fewer.

In assessing the need for Federal legislation, NRMA urges the subcommittee to ask whether there is actually a need for additional grants of enforcement authority beyond those which are provided under current law and, if so, whether the system of national enforcement by State attorneys general envisioned in this legislation is the most desirable alternative.

NRMA strongly supports allowing the Federal Trade Commission to have exclusive jurisdiction over the nationwide enforcement of telemarketing activity.

We do not object to the promulgation of a reasonable telemarketing rule.

Nationwide enforcement of any telemarketing legislation and subsequent rules should be under the Federal Trade Commission, which has the ability to develop and communicate a consistent nationwide enforcement policy. If the Commission needs additional modest resources to combat telemarketing fraud, then this should be done.

If further Congressional oversight indicates enforcement is not adequate, then a carefully expanded increase in enforcement authority, designed to include State attorneys general, under the FTC's control and direction, might be warranted.

We note that Senator McCain's bill authorizes the FTC to appoint State attorneys general to assist the Commission to enforce Commission rules when the public interest so requires. We view this expanded grant of enforcement authority, on a case-by-case basis, as a step in the right direction relative to the two other bills pending before the subcommittee.

However, we maintain that enforcement should be kept strictly under the FTC's control.

There are alternatives to H.R. 4101, and, while insufficient consideration, in our opinion, has been given to alternatives, such as bonding and/or registration requirements for telemarketers, there are a number of positive alternatives which are underway.

First of all, we have heard testimony earlier today about the cooperative multi-state automated telemarketing fraud data bank, which helps track down violators. Also we know that only 22 States have signed on to this effort and we think that its effectiveness cannot be properly judged until additional States have demonstrated interest in this experimental project.

We also know that States have enacted new telemarketing fraud legislation and that States have been pursuing illegitimate telemarketing more aggressively, and we know that the FTC has allocated increased resources to telemarketing fraud.

We applaud these efforts. They should be given an opportunity to prove themselves before hastily considered Federal legislation is enacted.

In summary, we support efforts to protect consumers from fraudulent telemarketers. The recent Federal and State activities will do much to attack telemarketing fraud, and we urge the subcommittee not to overreact.

Thank you very much.

[The statement follows:]

STATEMENT OF THE NATIONAL RETAIL MERCHANTS ASSOCIATION

The National Retail Merchants Association ("NRMA") respectfully submits this statement for the Subcommittee's consideration on the pending telemarketing fraud prevention legislation (H.R. 4101, S. 2213 and portions of S. 2326). NRMA is the nation's largest trade association for the general merchandise retail industry. Our members operate 45,000 leading department, chain, independent and specialty stores in all 50 states; employ more than three million people; and have an annual aggregate sales volume in excess of $175 billion.

This statement is also endorsed by the American Financial Services Association (AFSA). AFSA is the nation's largest trade association representing nonbank providers of consumer financial services. Organized in 1916, AFSA represents 572 companies engaged in the extension of consumer credit throughout the United States. These companies range from independently-owned consumer finance offices to the nation's largest financial services, retail and automobile companies. Consumer finance companies hold over $143 billion of consumer credit outstanding and over $38 billion in second mortgage credit representing one quarter of all consumer credit outstanding in the United States.

We strongly support appropriate efforts to address telemarketing fraud because, as legitimate telemarketers, we are also injured when fraudulent telemarketers create consumer distrust of telemarketing in general. However, it is our view that the current legislation does not accomplish its well-intended objectives and, by virtue of its overly broad provisions, is likely to create far more problems for legitimate businesses than it will solve. For these reasons we strongly urge that the Subcommittee carefully consider the effect of the pending legislation on traditional retailers and other legitimate businesses. Hasty enactment of this legislation should be avoided.

THE DEFINITION OF TELEMARKETING CONTAINED IN THE LEGISLATION IS OVERLY BROAD AND WOULD SUBJECT TO UNNECESSARY REGULATION VARIOUS MARKETING AND ADVERTISING PRACTICES WHERE TELEPHONE USAGE IS ONLY INCIDENTAL.

H.R. 4101, as recently passed by the House, defines telemarketing as "use of a telephone . . . to communicate an offer for sale or to complete a sale . . ." This definition is so broad that it would encompass many standard retail and other business practices. It goes far beyond what is ordinarily considered "telemarketing."

For example, it would cover all facets of catalog ordering by phone (including the common and incidental practice of providing a telephone order number in a retail store's newspaper advertising); arrangements made by telephone for the delivery or servicing of merchandise; many insurance transactions or stock brokerage activities; dealings by telephone between suppliers and vendors; automobile servicing where an offer to make unexpected additional repairs is conveyed by telephone; and all other business activities that ordinarily, or even incidentally, involve a telephone offer or sale. Indeed, according to the report which accompanies H.R. 4101, the only limitation on this extremely broad definition is the "occasional use of a telephone by a person to sell for example, his or her house or car...." In short, virtually all business transactions which involve the use of a telephone as a sales tool, and all related advertising and marketing practices, could be covered by the bill's definition.

THE LEGISLATION GRANTS EXCESSIVE AUTHORITY TO STATE OFFICIALS; ENCOURAGES INCONSISTENT ENFORCEMENT, AND WILL PRECIPITATE UNNECESSARY LITIGATION AGAINST LEGITIMATE BUSINESSES

H.R.4101 will grant numerous state officials (and others) the ability to dictate the advertising and marketing activities of any business using a telephone as a sales tool. As approved by the House of Representatives, the legislation would permit state attorneys general, various state officials and private parties (including competitors) to bring federal suits against parties engaging in telemarketing that is "fraudulent" (which is not defined in the legislation), or that violates a yet to be promulgated Federal Trade Commission rule. It is almost a certainty that all these parties will have differing views of what is in fact "fraudulent" or in violation of the FTC rule.

It is the apparent intention of this legislation to allow state attorneys general and other officials to bring civil actions against marketers outside their states as long as they "allege" that the telemarketing practice "affects" their state or its residents. This is a prescription for chaos. It will create a proliferation of inconsistent state enforcement activities and differing legal interpretations which will result in a legal nightmare for retailers, especially those which operate in a multi-state environment.

Congress must recognize that there are many, small single-state based retailers throughout the country which operate, not by using sophisticated marketing techniques, but by advertising in national and regional special interest magazines. While these small and medium size retailers comply with their own state's laws, it is unreasonable to expect any of them to track the legal activities or the opinions of attorneys general in all 50 states. Yet H.R. 4101 would require just that.

For example, an attorney general in Maine might allege that the failure of an out of state retailer to make a particular telephone disclosure adversely affects his state's citizens. If a suit on that basis were successful, all retailers who receive occasional calls from Maine residents would be forced to make such telephone disclosures. As a practical matter, because merchants do not always know the origin of their customers' calls, they probably would have to instruct their telephone operators to make the disclosure to all customers. The alternative, to ascertain the state of every caller and then determine and make appropriate disclosures to each, is simply beyond the ability of a typical small business. To ask small business telephone catalog operators to reconcile conflicting state disclosures for hundreds of different products, for thousands of different callers, in dozens of different states is impractical and unreasonable, to say the least. Yet H.R. 4101 would require it.

The proponents of this legislation claim that it will promote consistency. It will do just the reverse. Instead of being subject to the possibility of two levels of enforcement—lawsuits brought by state attorneys general at the state level and by federal authorities nationwide, as is the case under current law, H.R. 4101 would also subject legitimate retailers to federal lawsuits brought by state attorneys general from their own and other states as well as private party-initiated actions in federal court. Although the largest of the national retailers are currently subject to varying advertising and marketing requirements on a state-by-state or local basis, H.R. 4101 would add additional tiers of enforcement. Furthermore, it allows individual state attorneys general to pursue novel standards of enforcement on a fifty-state basis. In short, H.R. 4101 creates more avenues for inconsistent enforcement, not fewer.

While proponents suggest that there is precedent for state attorneys general and private parties to sue in federal court to enforce federal regulations, that precedent is minimal in comparison to the broad array of advertising and marketing practices that would be subjected to state and private scrutiny under H.R. 4101.

In assessing the need for federal legislation, we urge the Subcommittee to ask (1) whether there is actually a need for additional grants of enforcement authority beyond those provided under current law and (2) if so, whether the system of national enforcement by state attorneys general envisioned in this legislation is the most desirable alternative.

THE LEGISLATION FAILS TO PROVIDE EQUITABLE TREATMENT TO PLAINTIFFS AND DEFENDANTS

The legislation fails to provide equitable and balanced private enforcement incentives. Both H.R. 4101 and S. 2213 allow attorneys' fees and the cost of expert witnesses to be recouped by any person who successfully brings an action against a telemarketer. Unfortunately, the converse is not true.

The provisions for attorneys' fees will undoubtedly encourage lawsuits, but those legitimate telemarketers who ultimately prevail against these potentially subsidized plaintiffs will be prohibited from recouping the costs of their defense. Litigation is expensive for all parties; this one-sided arrangement should not be permitted.

THE FEDERAL TRADE COMMISSION SHOULD HAVE EXCLUSIVE JURISDICTION OVER THE NATIONWIDE ENFORCEMENT OF TELEMARKETING ACTIVITY

NRMA has no objection to the promulgation of a reasonable telemarketing rule. However, nationwide enforcement of any telemarketing legislation and subsequent rules properly should be established within the domain of the Federal Trade Commission which has the ability to develop and communicate a consistent, nationwide enforcement policy.

It is clear that fraudulent telemarketers must be stopped, but, ultimately, nationwide enforcement authority must remain with the Commission. Unfortunately, neither H.R. 4101 nor S. 2213 would provide for any effective national oversight of enforcement authority. Indeed, these bills' provisions would allow a state attorney general claiming ongoing harm to the public to file in federal court prior to even contacting the Commission.

If modest increases in resources are necessary in order to permit the Commission to combat telemarketing fraud, then those increases should be sought. But any legislative approach which will result in "balkanizing" federal enforcement policy should be rejected. If future congressional oversight indicates enforcement is not sufficiently vigorous, then a carefully expanded increase in enforcement authority designed to include state attorneys general under the Commission's control and direction might be warranted. But to do so now, before a rule has been formulated and without Commission oversight, would be premature and unwise.

By way of contrast, we note that Senator McCain's "Consumer Fraud Prevention Act" (S. 2326) would extend the Federal Trade Commission's Mail Order Rule to telemarketing. While that bill also has an overly broad definition of "telemarketing," it does provide a somewhat more balanced approach to enforcement. S. 2326 authorizes the Federal Trade Commission to appoint state attorneys general to assist the

Commission to enforce Commission rules when the public interest so requires. While this expanded grant of enforcement authority, on a case-by-case basis, is certainly a step in the right direction (relative to H.R. 4101 and S. 2213), NRMA maintains that, initially, enforcement should be kept strictly under the FTC's control.

THERE ARE PREFERABLE ALTERNATIVES TO H.R. 4101.

There are alternatives to the cumbersome plan envisioned in this legislation. While insufficient consideration, in our opinion, has been given to alternatives such as bonding and/or registration requirements for telemarketers, a number of positive alternatives is already underway. For example, the Federal Trade Commission and state attorneys general have recently initiated a cooperative attack on telemarketing fraud. Specifically, a multi-state automated telemarketing fraud databank has been established to collect data to track down violators. While this concept appears to have merit, fewer than half of the states have joined this effort. Therefore, its effectiveness cannot be properly judged until additional states have demonstrated an interest in participating.

In addition, several states have enacted new telemarketing fraud legislation while others have begun to pursue illegitimate telemarketers more aggressively. The Federal Trade Commission has also allocated increased resources to telemarketing fraud.

We applaud these efforts, and appreciate the care that has been taken to move deliberately in this area to avoid disrupting legitimate businesses while building an effective legal framework for ongoing enforcement. Care also must be taken not to deprive the public of services they want nor to stifle creative new services in the future. Therefore, these efforts should be given an opportunity to prove themselves before hastily considered federal legislation is enacted.

CONCLUSION

We support efforts to protect consumers from fraudulent telemarketers. We believe that recent increases in federal and state activity will do much to bring fraudulent operators to justice more swiftly and efficiently. But we urge the members of the Subcommittee not to overreact. As currently drafted, H.R. 4101 would greatly impair the retail industry's ability to offer consumers the convenience of legitimate telemarketing activities because it would unnecessarily subject legitimate businesses to frivolous and inconsistent lawsuits.

If congressional oversight reveals that federal legislation is necessary, we strongly urge that any grant of enforcement authority for any federal telemarketing fraud legislation and subsequent rule remain with the Federal Trade Commission rather than with the states or with private parties. Only in this way can consistent national enforcement policies and legal interpretations properly and fairly be achieved.

Senator GORE. Thank you.

I have some questions now.

Senator McCain, who was called to another obligation, hopes to return shortly. If he does not get back before the end of this questioning period, I hope that each of you will agree to respond to any questions in writing he might have.

First of all, Mr. Brosan, how much money is being lost each year by VISA and Mastercard because of telemarketing fraud?

Mr. BROSAN. We estimate, Senator, that our losses, very conservatively, are over $100 million per year.

We don't collect the figures as such, on telemarketing as opposed to fraudulent use of a credit card number. It is not segregated in that fashion.

So, by going out and polling randomly our members, some of our larger members and smaller members, we have come up with a conservative figure of $100 million a year.

Senator GORE. Now you have adopted operating procedures to alert member institutions and others to suspected telemarketing scams and to the problem in general.

Is that correct?

Mr. BROSAN. Yes, sir.

We have automated systems in place and we require other systems, such as merchant deposit screening, which would monitor the merchants' average daily deposits, the number of deposits and the amounts of deposits, as well as systems in place to detect fraudulent transactions, excessive fraudulent transactions, or charge-back at merchant locations.

Senator GORE. I take it that you believe these private efforts have had limited success?

Mr. BROSAN. Yes, they have.

Senator GORE. Why is the provision permitting consumers, financial institutions, and others to sue in Federal court so important to VISA and Mastercard?

Mr. BROSAN. We think because of the magnitude of the problem, as we have talked, and we see a private cause of action for the institutions to be a very effective and integral part of the legislation. By raising or by having a threshold of $10,000, we think that we are eliminating some of the frivolous or nuisance type suits.

But these guys are shrewd. They stay ahead of everybody, and we think that you need a combined effort of private cause of action along with State attorneys general and Federal rules to pursue them.

Senator GORE. The $10,000 limitation would not markedly detract from your ability to obtain the benefits you have cited, then?

Mr. BROSAN. No. It would not.

Senator GORE. In testimony that you presented on the House side, you stated that this private right of action should not provide a mechanism for the consumer who is merely dissatisfied with a purchase to initiate a private fraud action against a merchant.

In your opinion, is the language in the House-passed bill sufficient on that point to safeguard against those kinds of actions?

Mr. BROSAN. I am not an attorney, but perhaps our counsel could respond.

Mr. BALLEN. I am Robert Ballen, from Morrison and Foerster, Senator Gore.

We would certainly be amenable to further clarification, either in the legislation itself or the legislative history, to address that point specifically.

We would be glad to work with the subcommittee staff on that point.

Senator GORE. Thank you.

Again, I appreciate the spirit of cooperation embodied in that.

Now I take it that you also believe, Mr. Brosan, that the State statutes around the country are not adequate to deal with this problem.

Mr. BROSAN. That's right, Senator.

We believe that the resources available and the scattered differences within the statutes, that if they were brought together, on the Federal level, it would provide a much more effective means.

Senator GORE. Now VISA and Mastercard, as I understand it, have procedures for essentially holding the consumer harmless. Is that correct?

Mr. BROSAN. Well, we abide by the Federal and State laws that are in effect. They are the governing body.

Senator GORE. But you have to pass along to——

Mr. BROSAN. If the consumer, within the time restraints, reports, then he generally winds up with his money back.

Senator GORE. Many merchants are damaged by this, then?

Mr. BROSAN. The merchants in this area are the ones that are holding the bag.

What has happened is the telemarketers have become wise enough to the schemes that they no longer establish merchant relationships with our financial institutions. They go into what we call a "factoring" operation.

In other words, they will go and approach a legitimate merchant, who has a long-standing history with a financial institution, who stands in good stead, and they will say to him I'd like you to do me a favor. I'm new in the area—or some such excuse—and they'll say I'd like you to deposit my sales drafts for me until I can establish a relationship with a bank, and would you take 5 percent or 10 percent for yourself right off the top, which they do in this.

So the merchant sees that he can make a couple of bucks and he wants to be helpful. He goes ahead and he makes the deposits for these individuals.

Now, the next day, conveniently, this money is wired out at the telemarketers request to some other bank, and what happens is this fellow who took his commission of 5 percent or 10 percent winds up being charged back, because the card holder protests the charge. The issuing bank then charges back the merchant bank; the merchant bank then charges back its merchant for that amount of money.

Now, when this guy runs out of money, as often is the problem—they have filed for bankruptcy and been forced out of business—at that point the financial institution picks up the remaining losses.

Senator GORE. Are you aware of any cases where a merchant has had to go into bankruptcy because of this?

Mr. BROSAN. Yes, there are such cases.

Senator GORE. Would you give me an example?

Mr. BROSAN. We could give them to you in writing. I don't have them with me, but I could give them to you.

Senator GORE. All right.

Now VISA and MasterCard recommend that the legislation be amended to provide the Federal courts with exclusive jurisdiction over all private causes of action brought under the bill. Some might question this particular suggestion of a fear that it would produce a significant increase in the Federal court caseload.

What are your views with regard to that concern?

Mr. Brosan. Our views on that concern are, with a threshold of $10,000, we don't feel that it will be unnecessarily clogged, and we feel that, by bringing it to the Federal level and having all suits brought under S. 2213 into the Federal level, we are going to provide uniformity, and we are not going to have different precedents being set across the country. We are going to have one governing body of rules, that is, the Federal Rules of Procedure.

Senator Gore. Do you believe that the $10,000 limitation, in other words, would hold down the number of new cases in the Federal court system?

Mr. Brosan. Yes.

We believe that this is not going to be an independent operation. The attorneys general will be working in conjunction with the Federal Trade Commission and there will be some uniformity and there will not be an over-proliferation.

Senator Gore. Thank you.

Mr. Williams, you mentioned that you have attempted to educate consumers on ways to avoid telemarketing fraud.

In addition to the newsletters that you have provided to us, do you have any other examples of that effort?

Mr. Williams. Typically, we would distribute, through our marketing arm, stick-on labels of assorted various and sundry direct mail pieces, which the dealers can send to their end-users in statement mailings.

Senator Gore. Do they work?

Mr. Williams. Oh, yes they do. The main problem is with the end-users. They are not on alert that they are going to be receiving this type call.

Typically, they will receive that at a lunchtime, when the manager is at lunch and the receptionist is vulnerable, maybe with the promise of a new radio.

There are a number of things that we have done in addition to that, Senator, such as develop video training programs for our educational presenters throughout the country to show to end-users, such as Kiwanis groups or other types of social clubs, and these are made available to our members, so that they can not only be visible in their community but can alert the entire community that it is something that just comes out of the blue.

They are very professional, these people, with slick sales presentations and can dupe even the most professional person that you think would not ever become involved.

Senator Gore. You referred to NOMDA's computerized data base on telemarketing fraud. Is it connected to the FTC attorneys general system?

Mr. Williams. I know that there is a connection, but I would like to refer that to our General Counsel, because that has been developed in his base through our staff attorneys.

Bob, would you comment on how that works.

Senator GORE. Would you identify yourself, please.

Mr. GOLDBERG. My name is Robert Goldberg. I am General Counsel for NOMDA.

We are one of the participants in the FTC data base and do contribute close to—I think up to about 3,000 complaints now have been put into the data base from NOMDA.

As we said, we average about 80 a week.

Senator GORE. About 80 a week?

Mr. GOLDBERG. That is correct, Senator.

Senator GORE. What kind of fraud do most of your members complain about most frequently? Are the complaints primarily related to inflated prices, nondelivery of goods, or what?

Mr. WILLIAMS. The most typical is this.

Of course, we are interested in protecting the end-user, the consumer. But the direct result to an independent businessman is that the inferior supplies, to use one example that happened to my service department, related to me—a new $5,000 copies, less than six months old, when this customer had been duped by a fraudulent telemarketer, he installed some supplies and, due to the incompatibility, the stuff turned to about the consistency of molasses in the copier, resulting, in, I believe, as I recall, a $600 to $800 unnecessary repair bill to this end-user.

Those are the typical things: the exorbitant pricing through the misrepresentation of the yields or the amounts: the term "case" is used; and, as I alluded to, to the fraudulent telemarketer, the "case" may be two bottles, where the end-user is used to thinking in terms of a dozen bottles in the typical manufacturer's case.

Senator GORE. Presumably that has a negative impact on the relationship between your legitimate members and their customers.

Mr. WILLIAMS. Yes.

They are very good at misrepresenting themselves as the local dealer.

Senator GORE. Now why do you favor the grant of authority to the State attorneys general, rather than deputizing or giving the FTC an option to deputize them?

Mr. WILLIAMS. Again, our General Counsel has studied both these bills, Senator, and I would like to refer that to him, if you please.

Mr. GOLDBERG. Senator, we support both the use for the attorneys general and the private right of action. We think the problem is very widespread and needs all of the assistance that it can get to redress it.

I don't believe the deputization is sufficient. I think all of the attorneys general have an interesting in protecting the consumers of their States. Trough a concerted effort, along with a private right of action, we can eliminate telephone fraud in the United States.

But the FTC has not demonstrated that it can do it on their own, and I believe they should welcome our support and our assistance.

Senator GORE. Thank you.

Ms. Mullen, you say that legitimate telemarketers are negatively affected by this problem. I certainly agree with that. We want to be sure that any legislation targets only the offenders and helps the legitimate telemarketers.

Is the effect of fraud merely indirect in giving legitimate telephone marketers a bad name? Is that the primary problem that you face?

Ms. MULLEN. It is not only indirect, as far as bad press is concerned, Senator, but also in calling consumers to sell enhancement products for our clients. Our people receive negative reactions from customers, even though their call is legitimate and is being placed with the knowledge and authority of the clients that we represent.

So, it is not only indirectly. It is also directly.

Senator GORE. Under your association's guidelines, have you got a policy on hours of the day when calls should be made to consumers?

Ms. MULLEN. As stated in the Standards and Ethics Guidelines of the American Telemarketing Association, we do not set specific hours of the day. However, our people are asked to subscribe to the idea of common sense and common courtesy in the practice of their telemarketing.

Senator GORE. I thought you had guidelines suggesting that calls be made only between 9:00 a.m. and 9:00 p.m.

Ms. MULLEN. I'm sorry. Yes, between 9:00 a.m. and 9:00 p.m.

But as far as any other limitations, no.

Senator GORE. Do you think the FTC ought to consider hours of the day restrictions on unsolicited calls?

Ms. MULLEN. I do not think that the FTC—my personal feeling is that no further constraints should be adopted as far as the time of day for calling. I think that between the hours of 9:00 a.m. and 9:00 p.m., in whatever time zone the calls are being made to, is a sufficient timeframe, especially for the practice of legitimate telemarketing.

With fraudulent telemarketing, it does not matter what the FTC does at this point.

Senator GORE. What about computer generated calls?

The House passed bill provides for a study of computer generated calls, including an evaluation of whether the individual called ought to have the ability to terminate such calls.

Does the ATA have any guidelines or policies regarding computer generated calls?

Ms. MULLEN. The ATA represents not only actual telemarketing service agencies and in-house telemarketing centers, but also businesses that manufacture this particular product or types of this particular product.

My personal feeling is that I would have no problem with an investigation as to how this particular product is used. In my own company, we do not use it at all.

However, as an association representing not only the telemarketing vendors but also the suppliers of the equipment that we use, we encourage our members who produce or sell this type of equipment that it be used in the utmost of ethical manners.

Senator GORE. Mr. Altier, I may submit questions to you in writing, because I have exceeded my time and Senator McCain has returned. I want him to have an opportunity with this panel.

Senator McCain.

Senator McCAIN. Thank you, Mr. Chairman.

I would like to thank the panel very much for a broad spectrum of views here that has been presented, which I think are very helpful, and will perhaps help us arrive at some consensus. I think we are all in agreement that something needs to be done. The question is the methods that need to be used.

Perhaps I could very briefly run through the panel three or four questions concerning how they feel about key aspects of this legislation.

Perhaps I could start from my left and go to my right, very briefly.

The definition of telemarketing in the bills says "the use of a telephone in the ordinary course of business to communicate with a person an offer for sale or to complete a sale of a product or service," the definition is so broad that it may encompass most businesses, not just telemarketers.

Do you agree with that?

Mr. ALTIER. Absolutely. It is very broad.

If you examine the House approved bill, as well as the report that accompanies the bill, any business use of the telephone, in the ordinary course of business and even incidental use would be covered. The only exclusion in the House approved statutory language is the occasional use of a telephone by a person to sell, for example, his or her house or car. That is the only limitation.

I agree with you that it is overly broad. If the legislation goes forward, something should be done to narrow that down significantly.

Senator McCAIN. Ms. Mullen.

Ms. MULLEN. I totally agree.

Senator McCAIN. Mr. Williams.

Mr. WILLIAMS. Yes. I think there needs to be some clear guideline, especially since we are talking about the fraudulent use of the telephone.

Senator McCAIN. Mr. Brosan.

Mr. BROSAN. Senator, we feel that the definition is fine the way it is and that by narrowing the definition, we are perhaps creating loopholes for these very ingenious and unscrupulous telemarketers to skirt the law.

Senator McCAIN. Thank you. Now we will start with you and go back in the opposite direction.

The provisions in S. 2213 and H.R. 4101 that would permit the attorney general and private suits based on the allegation that a particular practice is "fraudulent and dishonest"—some suggest that these standards are too vague.

Mr. BROSAN. No. I may be misunderstanding your question, but we don't think so.

Senator McCAIN. Either "fraudulent and dishonest" or "fraudulent"—some suggest that these standards are too vague.

Mr. Williams, would you comment?

Mr. WILLIAMS. I think our association definitely supports the attorney general use and the private right.

Ms. MULLEN. I'm sorry, Senator, but I don't understand the question.

Senator MCCAIN. The provisions in S. 2213 and H.R. 4101 would permit the attorney general's and private suits based on the allegation that a particular practice is "fraudulent and dishonest"—that is the way it is described in S. 2213, or just "fraudulent" as it is described in H.R. 4101. Is that standard too vague to allow the AG and private suits to bring a suit or private suits to be brought?

Ms. MULLEN. As I stated in my testimony, the American Telemarketing Association recommends that all of prosecution and enforcement, whichever format the final legislation has that passes, be coordinated through the Federal Trade Commission.

Senator MCCAIN. Mr. Altier?

Mr. ALTIER. The standard "fraudulent and dishonest" was in the original Luken bill. "Dishonest" was subsequently deleted as it went through the House.

They eliminated the "dishonest" standard because we argued that it could mean just about anything and that there was not any basis for it to remain in the bill. Both terms are also in S. 2213.

At the very least we argued that"dishonest" should be eliminated. With regard to "fraudulent," there is some body of law out there as to what "fraudulent" means. But certainly there are some gray areas. As legislation goes forward, "fraudulent" could be more precisely defined.

Senator MCCAIN. Thank you.

Not exactly on the subject, Mr. Brosan, but I guess that is a privilege of the committee, it disturbs me that con artists are able to become credit card members. To what extent do you review the financial and business background of companies?

Mr. BROSAN. There are regulations which are promulgated by both associations, Mastercard and VISA, which require financial backgrounds and credit checks on the merchants that they are to sign, to include income tax, if it is permissible within the States that they are in.

They are also required to make a personal visit to the location of that merchant, on premise, and to look at that, and to check references to see if this merchant or the principal involved has been terminated by a bank for fraudulent activity in the past.

Now, there are systems in place, automated systems also put into place. We discussed this just a little while ago. There are merchant deposit screening methods, which would screen the average dollar value of the merchant, the number of tickets he submits a day, in order to point out any dramatic rise in his deposits or amount of deposits. This causes an investigation to come back.

There are automated systems in place to monitor the number of fraudulent transactions going through the business, which cause an investigation to come back.

What has happened is the financial institutions have been monitoring and the fraudulent telemarketers are well aware of that. What they have gone to now is what I referred to in my original testimony as "factoring." This is where the telemarketer does not establish a relationship with a bank, a merchant relationship with a bank, but, rather, goes and finds a legitimate merchant who is out there and has an established relationship with a bank—he goes to him and says you do me a favor. I have not gotten a bank yet. I am new in the area. Would you deposit my sales drafts for me, and you can have 10 percent for yourself for the trouble of depositing these.

The merchant then goes ahead and deposits those sales drafts for whatever amount of money it is. He has been instructed by the telemarketer to wire the money the next day to a bank account in another State. What happens then is the card holder gets the charge on his bill. He protests to the issuing bank. The issuing bank charges back the merchant bank and the merchant bank charges back that merchant for the full amount of those deposits, in excess of the 10 percent that he took off the top.

Unfortunately, what happens is this good merchant, who thought he was going to just make a couple of bucks on a business deal, winds up going into bankruptcy, and after he is out of business, then the merchant bank starts suffering the losses also.

Senator McCAIN. Thank you very much.

Thank you, MR. Chairman.

Senator GORE. Thank you.

Thank you all. We would spend more time with you except for the time crunch.

We appreciate your appearance here today.

Let me call now on the last panel of witnesses: Ms. Jane King, Deputy Director of the National Consumers League; Mr. Robert Levering, Vice President for Government Affairs and Legislative Counsel with the Direct Marketing Association; and Dr. John Renner, Department of Community Health, Trinity Lutheran Hospital in Kansas City, Missouri.

We are delighted to have the three of you here.

Without objection, your prepared statements will be included in the record in full, and we invite you to proceed with a five minute summary of your statements.

Ms. King, we will begin with you.

Welcome, and please proceed.

STATEMENT OF JANE KING, DEPUTY DIRECTOR, NATIONAL CONSUMERS LEAGUE

Ms. KING. Mr. Gore and members of the subcommittee, I am Jane King, Deputy Director of the National Consumers League, which is the pioneer consumer organization in the country.

The League, as a national membership organization, is involved in research, education and advocacy on behalf of consumers in matters requiring Federal legislative and regulatory decisions and actions.

On behalf of the League, I would like to thank you for the opportunity to present our views today.

I would like to note that it is part of our testimony that we comment on the provision in S. 2326 that endorses the concept of an FTC study of life care homes, also known as life care communities.

We have previously testified before the Federal Trade Commission that we think this is a very serious consumer problem, in part due to fraudulent activity in the States and in part due to mismanagement.

It is high time that not only a study be made but Federal rule making procedures be established if the problem is not soon corrected in the States.

In terms of telemarketing fraud, Esther Shapiro, Director of the Detroit Consumer Affairs Department and also League Vice President, indicates the depth of the problem for her office in a letter she wrote recently to NCL. She said: "The time spent in providing information and following up complaints on telemarketing fraud is my department's major burden. We spend an inordinate amount of time dealing with people who are questioning the offers they receive. The strange aspect to this is that they call because they feel the offers they receive are not quite legitimate; yet, when we urge them to ignore the calls, it starts an argument: "If it's not honest, how can they get away with it?"

She continues: "The rest of our time is spent in a fruitless attempt to recoup lost money, since almost all of these offerings are carried across State lines and because the perpetrators move very quickly, this is always an exercise in futility. Legislative reform," she says, "on a national level is badly needed."

Ms. Shapiro went on to state that she does not think the problem will be resolved until many more resources are put into enforcement efforts.

In response to this kind of need to offer greater protection to consumers, the League participated in hearings held by the House Subcommittee on Transportation, Tourism, and Hazardous Materials, and helped to develop and introduce the bill, which was introduced by Representative Luken.

The League supports the Luken bill and supports the parallel provisions in SS. 2213 and S. 2326.

Though the Federal Trade Commission is the logical Federal agency to lead a concerted Federal effort to fight telemarketing fraud, the current FTC does not have the adequate resources to perform the job effectively—or I don't think we would be sitting here today.

The League urges Congress to review the mandate of the FTC, the levels of staffing, and the resources assigned to each area of responsibility.

As you heard already, the data bank, which, to my knowledge, has been at least five years in development, still only has 17 States contributing information and is not functioning at a greater level because it is under-financed.

I think right here we see part of the key to the problem.

As a result of this assessment of the FTC's capacity, we support the provisions in S. 2213 and H.R. 4101, which would give the States attorneys general the authority to bring a civil suit against fraudulent telemarketers under the FTC statutes.

As was stated earlier by Attorney General Stephan, precedent for sharing enforcement with the States and private parties exists in the enforcement structure of several Federal Government agencies.

We also think that this will be an effective method because other States may also intervene in such actions in a simultaneous fashion.

Also, to broaden the potential for action against telemarketing fraud, the League also recommended and supports the right of citizens and others, such as financial institutions, to bring an action against a fraudulent telemarketer under the FTC statutes.

We support these and also the promulgation of the rule by the FTC because of the overriding frustration of the many consumers who have been victimized by telemarketing fraud and a rather cynical attitude that is developing out in the hinterlands about what can be done with it.

We receive calls, consumer agencies receive calls, and the BBB receives calls, and we all have to say if you have been scammed, sorry, but we cannot give you much hope about what will be done. And we also know that there is a huge necessity for much more consumer education, which all of us here, I think, are trying to undertake, so the consumers will know the rules of the road in telemarketing, because it is a burgeoning and important business tool, but one many, especially older, consumers are not used to.

Thank you for this opportunity.

[The statement follows:]

STATEMENT OF JANE M. KING, DEPUTY DIRECTOR, THE NATIONAL CONSUMERS LEAGUE

Mr. Chairman and members of the subcommittee, I am Jane King, deputy director of the National Consumers League, the pioneer consumer organization in the country. The League, as a national membership organization, is involved in research, education and advocacy on behalf of consumers in matters requiring federal legislative and regulatory decisions and actions. On behalf of the League, I would like to thank you for the opportunity to present our views to you today.

Our concern with telemarketing fraud developed from our work related to investment fraud with the Commodity Futures Trading Commission, the Better Business Bureau and the American Association of Retired Persons. During the past year, the League has prepared films and printed materials to educate the public about telemarketing fraud. The League shares the concern of this subcommittee that "boiler room" phone operations are a key ingredient in many kinds of scams. Telemarketing fraud is a significant and costly presence in the marketplace today, in part because telemarketing is an increasingly important sales mechanism for many reputable businesses. What makes telemarketing fraud a bonanza for con artists is the ease of setting up a boiler room and the jurisdictional escape hatch which allows offenders, at the first sign of legal action, to skip town and move their "shop" to a different state.

Esther Shapiro, Director of the Detroit Consumer Affairs Department and League Vice-President, indicates the depth of the problem for her office in a letter to NCL. She said, "The time spent in providing information and following up complaints on telemarketing fraud is my department's major burden. We spend an inordinate amount of time dealing with people who are questioning the offers they receive. The strange aspect to this is that they call because they feel the offers they receive are not quite legitimate, yet when we urge them to ignore the calls, it starts an argument: 'It it's not honest, how can they get away with it?' "

She continues: "The rest of our time is spent in a fruitless attempt to recoup lost money. Since almost all of these offerings are carried across state lines, and because the perpetrators move very quickly, this is always an exercise in futility. Legislative reform, on a national level, is badly needed." Ms. Shapiro went on to state that she does not think the problem will be resolved until more resources are put into enforcement efforts.

Telemarketing fraud comes in many disguises, but its practitioners are particularly adept at exploiting several sales avenues at once to land a victim. Unfortunately, Americans are easy prey because we assume we have consumer protection statutes that protect us from misrepresentation and fraud. We tend to think that ads have been approved by someone, that businesses are licensed, that requests for a credit card number come only from valid businesses. In other words, most of us act in good faith and assume the good faith of others. Sadly, the tactics of con artists could undermine the faith of Americans in the reliability of telemarketing if we don't become more adept at curbing the abuses.

In response to the need to offer greater protection to consumers, the League participated in hearings held by the House Subcommittee on Transportation, Tourism and Hazardous Materials, as the Telemarketing Protection Act of 1988 was developed and introduced by Representative Luken. The League supports the Luken bill and supports the parallel provisions in Senate Bills S. 2213 and S. 2326.

Though the Federal Trade Commission (FTC) is the logical federal agency to lead a concerted federal effort to fight telemarketing fraud, the current FTC does not have the adequate resources to perform the job effectively. The League urges Congress to review the mandate of the FTC, the levels of staffing and the resources assigned to each area of responsibility with a view toward restoring its capacity to monitor the marketplace. At best, the FTC is limping along, a victim of budget cuts and a lack of commitment from an Administration that has espoused across-the-board deregulation.

To expand the capacity for action against fraudulent telemarketers, the League supports the provisions in S. 2213 and H.R. 4101 which would give the states' attorneys general the authority to bring a civil suit against fraudulent telemarketers under the FTC statutes. Precedent for sharing enforcement with the states and private parties exists in the enforcement structure of the Commodity Futures Trading Commission and in the National Highway Traffic Safety Administration in cases of odometer fraud. Enforcement of federal antitrust and some environmental laws is also shared with the states and private parties.

In these proposals, the role of the FTC in acting against telemarketing fraud remains central. The FTC must be given written notice of state actions thirty days prior to its commencement or as soon as practicable if the action is urgent and may intervene in such actions.

Other states may also intervene in such actions if they are affected by the same fraudulent telemarketing operation. Because the action against telemarketing fraud is so often left to the states, it is imperative that the states whose citizens are victimized be able to move against a defendant in another state.

To broaden the potential for action against telemarketing fraud, the League also recommended and supports the right of citizens and others such as financial institutions to bring an action against a fraudulent telemarketer under the FTC statutes in a district court of the state having jurisdiction of the defendant. As both S. 2213 and H.R. 4101 establish, the FTC could be a party or intervenor in such action and must receive written notice thirty days prior to the commencement of the action.

S. 2213, H.R. 4101 and S. 2326 direct the FTC to promulgate a Rule governing telemarketing activities. All three proposals leave some discretion to the FTC as to the exact nature of the Rule. All would require refunds within a specified period. S. 2213 and S. 2326 would require a 3-day cooling off period when a prize is offered, a concept the League endorses. H.R. 4101 would require the FTC to define cancellation rights, also a proposal that the League endorses. S. 2213 and H.R. 4101 would amend the FTC Act to make it an unfair or deceptive act or practice for a telemarketer to engage in harassment, oppression or abuse in the conduct of business, an important additional protection for consumers.

NCL recommended and supported the creation of an FTC clearinghouse to provide information to persons making inquiries about telemarketers. Because fraudulent operators move around so often, consumers need ready access to up-to-date information on companies or organizations persons who contact them by phone. A federal clearinghouse could also provide information to the public about trends in telemarketing fraud, so that consumers could be advised of ways to distinguish the legitimate from the fraudulent company or sales person.

S. 2326 addresses health quackery, life-care communities, and telemarketing fraud. Two provisions of the telemarketing section concern the League. The League has concluded that the amendment entitled "Postal Data" would confer on the FTC an additional authority that could unduly interfere with the privacy rights of citizens. The League also does not see the necessity to include the "Financial Data" section, since that authority is already available to the states' attorneys general.

The League fully endorses, however, the provision in S. 2326 that would require the FTC to conduct a study of unfair or deceptive acts or practices in the life care home industry, and to initiate a trade regulation rule proceeding if its is warranted. As the publisher of *A Consumers Guide to Life-Care Communities,* the League is aware of the fraud and financial mismanagement that has occurred in the industry.

In a hearing before the FTC on March 16, 1988, the League stated to the Commission that, "The Federal Trade Commission has an obligation to examine the capacity of the states to establish the appropriate standards for financial and contractual integrity and soundness, for appropriate disclosures to consumers about finances and all terms and conditions of the contracts, and to provide the requisite enforcement capacity. The financial and contractual arrangements of continuing care communities are complex, an amalgam of real estate, nutrition, health care and other industries. These mixed marketplace characteristics create a confused regulatory environment that should be carefully scrutinized by the FTC to assure that consumers are adequately protected against financial failure or deceptive practices in the industry."

Thank you again for this opportunity to express the League's views on these important legislative proposals. American consumers assume that their government protects their rights at the marketplace. In the case of protection against telemarketing fraud, the current protections all too often look like a farce to the victim. In the case of the expansion of life-care communities, it is critical that the FTC establish a presence to assist the states in assuring elderly Americans that their investment in life-care will be sound.

Senator GORE. Thank you very much.

We will hold our questions until the other two witnesses have completed their statements.

Next is Mr. Robert Levering, Vice President for Government Affairs, Direct Marketing Association.

Mr. Levering, welcome and please proceed.

STATEMENT OF ROBERT LEVERING, VICE PRESIDENT FOR GOVERNMENT AFFAIRS AND LEGISLATIVE COUNSEL, DIRECT MARKETING ASSOCIATION

Mr. LEVERING. Thank you, Mr. Chairman.

DMA appreciates the opportunity to testify. The consumer protection record of our association is well known to this subcommittee. I don't want to take the time to review it.

Let me just say that only about one-tenth of our 3,000 corporate members are traditional telemarketers in the sense of the service bureaus and those that sell almost exclusively over the phone.

However, because of the breadth of the definition in the legislation, virtually all of our members would be affected, and that includes nonprofits and cataloguers and printers, banks and credit card people, et cetera.

My first comment is when we heard about the Telemarketing Fraud Prevention Act, we expected to be able to support it wholeheartedly. That is because businesses suffer truly as much as consumers do, and, within our own membership, we have three kinds of victims.

First of all, we have the business consumers. We have many of those.

We have the credit card companies and the banks, who are members of ours also, who are suffering because of the charge-backs. You have already heard testimony on that.

Then we have the telemarketing community and the cataloguers, who all suffer from the poisoning of the well, if you will, the bad name that the fraudulent operators bring to the business.

So we would be delighted to support this legislation. In fact, we think the business community should be marching shoulder to shoulder with consumers. They are not.

The subcommittee is aware of the resistance and of the concerns of some in the business community, in fact, of many organizations. I would like to discuss this briefly.

There are a number of problems with H.R. 4101, many of them of the minor variety.

Let me just focus on our main concern, which is the Federal grant of Federal authority to the State AGs.

Let's just take an overall look at the problem.

Even if the definition of telemarketing were narrowed—and we do support that—there is a problem defining it so that there are no loopholes.

We, under normal circumstances, would support a fairly broad definition of telemarketing if there were sufficient safeguards for legitimate marketers.

We would also support fairly vague terms, like "fraudulent," because, even though that is open to interpretation, you need that kind of flexibility when dealing with these slippery con artists.

Under current law there are only a number of Federal agencies, mainly the FTC, that have the authority to interpret in an enforcement action those vague terms and have a meaningful effect on national marketers.

We would support an extension of their authority. We would support an extension of their manpower reserves.

On the other hand, we do not want a fragmentation of the Federal power, so that we have to look to 50 different States to figure out what is predictable, in terms of the law.

Every time a new marketing item comes up, a new plan or any new marketing idea, it has to be reviewed. If the review takes into account just the Federal law and the body of case law that supports it and the safeguards that are present within the FTC, that's fine.

I might mention that Senator McCain's bill does contain these safeguards because it focuses the initiation of the lawsuits on the FTC, where we have always looked for that authority.

And there is the additional risk of misguided lawsuits. And I do not mean the AGs running wild.

I understand that that might be a concern for some. DMA and our members have had a fine relationship with the State AGs for many years. But I think the seat belt analogy is appropriate here.

Even though I trust a driver that I might be driving with and I think that traffic accidents are very rare, I still want to put a seat belt on and I don't want to drive on a continual basis in a car or vehicle that does not have a seat belt.

Although national marketers who are legitimate are not the target of this legislation, we are along for the ride. Because we are along for the ride, we don't want to be in a vehicle without proper safeguards, even though we trust the drivers, as much as you can trust anyone, and we know that accidents are few and far between. The risk of a mistake that affects your entire national marketing plan is just too great.

We can willingly support effective and safe legislation and we expect to do that. As a matter of fact, we think that any legislation in this area should begin with the six items that the FTC has requested to augment their own authority, and they have documented why they need that. We also fully support the right of credit card companies to sue in Federal court and to recover damages that accrue in the charge-back situation.

We think this can be done with a rifle shot and not by allowing private right of action. This, after all, is only a logical extension of the "holder in due course" doctrine, which was meant to give the credit card people the incentive to pursue the businesses because they have the leverage.

The loophole here is that when there is not a continuous business relationship between the credit card company and the marketer because they go out of business, then they ought to be allowed to sue in Federal court, and we do support that.

We think, however, that the first response of the Congress to this problem should not be a wholesale grant of Federal authority to the States.

Thank you.

[The statement follows:]

STATEMENT OF ROBERT LEVERING, VICE PRESIDENT FOR GOVERNMENT AFFAIRS AND LEGISLATIVE COUNSEL FOR THE DIRECT MARKETING ASSOCIATION

Good afternoon, my name is Robert Levering and I am vice-president for government affairs and legislative counsel for the Direct Marketing Association. I am testifying on behalf of the association and its more than 3,000 members. We appreciate this opportunity to comment on the 3 bills before the subcommittee dealing with the problem of telemarketing fraud: H.R. 4101, S. 2213, and S. 2326.

BACKGROUND ON DMA AND DMA'S SELF REGULATORY PROGRAMS IN THE TELEMARKETING AREA

DMA is the largest trade association representing marketers that utilize the U.S. mail, telephone, television, and other electronic media to offer products and services directly to the American public. Over 100 DMA members are traditional telemarketers or telemarketing service bureaus that perform marketing functions for others. However, because of the broad definition of telemarketing in the legislation before this subcommittee, virtually every one of the 3,000 corporate members of DMA could be affected by it. Our diverse membership includes catalogers, mail order companies, financial service marketers, charitable fundraisers, non-profit marketers, political organizations, magazine publishers, and book and record clubs as well as printers, advertising agencies, list brokers, mailing houses, and other suppliers.

Telemarketing fraud is a major consumer problem and it is a problem for businesses as well. Although they are only a small minority among telemarketers, fraudulent operators do great damage to legitimate businesses. They steal sales based upon deception and poison public perception of telemarketing generally. Therefore, DMA has taken every opportunity to combat this problem through industry self-regulation, consumer education, and support of effective legislation.

DMA has gone as far as the anti-trust laws allow in establishing and implementing industry ethical business standards. In addition to the DMA *Guildelines for Ethical Business Practice* governing direct marketing activity generally, the association's Telephone Marketing Council in 1983 assisted in the development of specific *Guidelines for Telephone Marketing*. These guidelines outline the responsibilities of DMA and telephone marketers to the consumer, the community, and the industry. Copies of these guidelines are being submitted alone with this testimony. The guidelines are also part of the direct marketing industry';s general philosophy that self-regulatory measures are preferable to governmental mandates whenever possible. Self-regulatory measures are more readily adaptable to changing techniques, economic and social conditions, and encourage widespread use of sound business practice. The Guidelines are administered by two DMA Committees, the Committee on Ethical Business Practice and the Ethics Policy Committee.

The Committee on Ethical Business Practice was established by DMA to investigate and examine mailings and offerings throughout the direct marketing field. This is done in an effort to increase good business practice for the direct marketing industry as well as to provide a consumer protection device. Complaints are referred to the Committee by consumers, action line reporters, and industry members. In cases involving possible law violations and a lack of company cooperation, the complaint files are turned over to the Federal Trade Commission, the office of the attorney general in the marketer's home state, U.S. Postal Inspection Service and other law enforcement agencies.

DMA's Ethics Guidelines are reviewed and updated by the Ethics Policy Committee. The Policy Committee also has the responsibility of overseeing DMA's self-regulatory programs and consumer and industry education efforts.

In addition, DMA cooperates with consumer and regulatory agencies in identifying fraudulent operations. This includes providing input into the FTC/NAAG Telemarketing Fraud Database. Finally, DMA recognizes that the best weapon against any fraudulent business conduct is an informed and vigilant consumer public. To this end, DMA has committed extensive association resources to enducating consumers on how to protect themselves from being defrauded by unscrupulous telephone marketers. DMA has produced and distributed consumer tips to action line reporters and developed and distributed pamphlets such as the *Guidelines For Telephone Shopping*, produced in 1985 in cooperation with the United States Office of Consumer Affairs. Copies of this and other materials will be provided to this subcommittee.

DMA'S COMMENTS ON THE LEGISLATION

For simplification, we will direct our testimony to the provisions of H.R. 4101 because it has had the benefit of the most legislative work. Chairman Gore's bill, S. 2213, is an earlier version of H.R. 4101, and committee staff has indicated that the current version should be considered a rough draft, Senator McCain's bill, S. 2326, is a much more comprehensive bill dealing with fraud problems of the elderly. I would like to comment on one aspect of S. 2326 in discussing options for expanding the powers of state attorneys general.

Even though we believe that there are no provisions in H.R. 4101 that would be truly effective against fraudulent telemarketers, DMA would like to be supportive, and only one provision prevents us from being able to support this bill—the granting of federal authority to state attorneys general and other state consumer protection officials.

The genius of federalism has served this country well in many areas, spawning a myriad of approaches to government and providing a testing ground for novel ideas. National marketers, such as DMA members, are perhaps the group most burdened by this diversity of rules and enforcement theories across the country, but we have been able, for the most part, to find reasonably efficient ways of coping with this diversity. However, if elected officials in every state were to have the power to give nationwide effect to their views on what is fraudulent, this would increase the risk of doing business in a national market since the ground rules could be affected by 50 different sources and the chance of a misguided enforcement action doing serious damage would be greatly expanded.

Today the only agencies that can impose nationwide injunctions on American businesses are federal agencies such as the Federal Trade Commission. The FTC has established procedures for approving complaints before they are filed. In addition, a whole body of law exists that informs these enforcement decisions while at the same time giving notice to the business community of the kinds of marketing activities that are likely to be considered deceptive or fraudulent. In the granting of federal authority to state officials in H.R. 4101 we see none of these safeguards.

For legitimate businesses this would be like riding in a car that has no seat belts. It's not that accidents are all that common or that we distrust the new drivers, but it would not be prudent to go for a ride in a vehicle without proper safeguards. The bill calls for discretionary intervention by the FTC in federal actions brought by state officials to guard against inconsistent or erroneous interpretations of federal standards. This provision, however, is a totally untested airbag; and we have no way of knowing whether it will open when we need it or whether it will provide protection if it does open.

The House staff is convinced that there is precedent for the granting of federal authority to state officials in the Commodities Futures Trading Act (CFTA). However, this is in reality no precedent at all. We don't know from CFTA experience how safe it is for state officials to initiate federal actions because it has never been done in the 10 years since independent state actions were permitted by amendment to the CFTA. States have always joined in federally initated law suits and have never gone forward on their own.

Unlike the esoteric area of commodities futures trading, where deference to federal expertise is to be expected, telemarketing fraud is an area where every law enforcement official could be willing to file suits based upon his or her own understanding of what is fraudulent. In fact, that is the idea behind this provision to permit independent and rapid enforcement action by state officials. It is important that Congress recognize that the CFTA gives no guidance as to how this will work or how risky this blanket grant of federal authority would be. As a practical matter, this provision is without precedent.

In addition, the effectiveness of this controversial provision has been overestimated. Nationwide remedies in the hands of state attorney generals would merely force fraudulent telemarketers to conceal their ill-gotten gains more quickly and to change their scams more often, and they have shown themselves fully capable of both. At the same time the option of federal civil suits will distract state law enforcers even more from the only truly effective response to fraudulent operators—state criminal prosecution.

This is not to say that there are not other problems with H.R. 4101. There are, but they are comparatively minor ones. The bill mandates the most abbreviated form of FTC rulemaking to deal with very complex and controversial issues; it opens up the federal court system to lawsuits from private citizens, business customers, and competitors at a time when Congress is considering raising the federal jurisdictional threshold from $10,000 to $50,000 to relieve the overburdened federal judiciary; and it creates a federal cause of action for harassing consumers by phone on the theory that telemarketing is similar to debt collecting by the telephone. DMA's concerns in these areas are explained in more detail below.

FTC Rule Making.—H.R. 4101 would require the Federal Trade Commission to issue a trade regulation rule within 180 days of enactment of the legislation. This expedited rule making procedure is used by the commission and was designed to be used by the commission when dealing with relatively simple, non-controversial issues. Such is not the case here. H.R. 4101 would mandate that the commission consider issues and specific provisions which are complex and controversial. Here are some of the specific provisions that the bill would have the FTC consider in its rule making procedures along with the DMA's comments:

1. Extending the 30 Day Mail Order Rule to sales consummated over the telephone. DMA's *Guidelines for Telephone Marketing* have long recommended that telemarketers abide by this rule even though it does not now specifically apply to telemarketing. DMA would support the formal extension of the Mail Order Merchandise Rule to include telephone sales as long as the terms and provisions are identical to the existing rule to avoid confusion for businesses and consumers. We would also regard this as an appropriate issue to be dealt with in an expedited 180 day rulemaking proceeding.
2. Giving consumers a period, similar to the 3 day cooling off period for door-to-door sales, during which they might cancel a sale entered into over the phone. The vast majority of DMA members would have no problem with this provision except to the extent that it might interfere with expedited delivery of customers' orders. There are some products and services, however, for which a 3 day cooling off period would be highly inappropriate, such as the telephone sale of stocks and other investments.
3. Requiring notice to telephone consumers of their right to cancel. This is not specifically mentioned in H.R. 4101, but it is an inevitable issue once a customer cancellation right is granted. The FTC and consumer groups are going to want to know how consumers will know if they have a right to cancel. Suffice it to say that designing an effective notice requirement that does not interfere with legitimate telemarketing is an extremely complex and controversial topic that should not be tackled in an expedited rulemaking proceeding.
4. Prohibiting harassing or abusive language by telemarketers. What is harassing or abusive is an extremely subjective concept, and the guidance given in the Fair Debt Collection Practices Act is not always relevant to a marketing situation. Here again we trust the Federal Trade Commission's ability to sort out what practices should or shouldn't be prohibited, but we question whether an expedited proceeding is either wise or necessary (especially since this area, like the other complex areas, has little or nothing to do with the fraud problem).
5. Limiting the hours during which telemarketers may solicit consumers. What consumers consider to be reasonable hours can vary greatly from region to region within the United States, and it certainly is not the same for a farmer as it is for a city worker. This does not seem to be an area amenable to federal rulemaking of any sort.

Private Right of Action.—DMA strongly supports the right of Master Card and Visa to sue in federal court when they have been injured by the failure of a telemarketer to cover charge backs by customers. This is a natural extension of the changes in the Holder in Due Course Doctrine effected in the mid-70's, and should most appropriately be dealt within specific legislation in that area. However, DMA supports the current provision as doing more good than harm. The problem with the Private Right of Action provision is that by offering the possibility of attorneys' fees (for prevailing plaintiffs only), the bill provides an incentive to disgruntled customers or competitors to file suits for the purpose of annoyance or to force a settlement. Even with the $10,000 threshold, these nuisance suits could still be filed by suppliers, business customers or even competitors on the basis of alleged fraudulent activity using the telephone. Thus, it would be preferable to enact separate legislation in the Holder in Due Course area for the benefit of credit card companies that do not have the leverage over fraudulent telemarketers that the law intended because they do not have the ongoing business relationships with banks that the 1970 amendment contemplated.

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H.R. 4101 has many problems, but only one is serious enough to prevent DMA from supporting legislation that might do some good in reducing the telemarketing fraud problem. That one provision is the one which would give state officials the

power to go into Federal court and seek nationwide remedies for alleged fraudulent practices involving the telephone.

Other provisions in H.R 4101 we could live with, and some we would actively support. For example, we support the extension of the Mail Order Merchandise Rule to telemarketing (recognizing, however, that this will not affect the fraud problem), the right of credit card companies to sue fraudulent telemarketers in federal court to recover customer chargebacks, and a number of provisions not included in any of the bills. These are detailed in the testimony of the Federal Trade Commission. There are six specific provisions which the commission feels would aid their efforts to combat telemarketing fraud, and we do not see any reason why these provisions should not be the starting point for effective legislation.

DMA is very interested in doing what can be done through legislation to combat the problem of telemarketing fraud, and we stand ready to work with this subcommittee to develop effective legislation. All of the bills before the subcommittee today have problems that demand more attention than is available in the waning days of this session. If adequate time is taken to develop an anti-telemarketing fraud bill, DMA is confident that we can whole heartedly support the result and that it will be more effective and less risky than the current bills.

Senator GORE. Thank you.

Dr. John Renner is our final witness. Dr. Renner is from the Department of Community Health at Trinity Lutheran Hospital in Kansas City, Missouri.

Welcome and please proceed.

STATEMENT OF DR. JOHN H. RENNER, DEPARTMENT OF COMMUNITY HEALTH, TRINITY LUTHERAN HOSPITAL

Dr. RENNER. Thank you, Senator Gore, Senator McCain.

I am a family physician and I run a resource center on health fraud. We get reports from all over the United States.

I recently have been co-chairman of a conference on health fraud, quackery and misinformation that was a Food and Drug Administration sponsored national meeting.

My comments are not limited to my experiences just in the State of Missouri.

I also have had the opportunity to get inside the camp of the enemy. In the field of health, you may be surprised to know that there are actual groups training people how to sell quackery and health fraud. They are very much aware of telemarketing and of satellite television transmission and cable transmission.

By posting an 800 line, they make it very easy for the victim to get in touch with the "quackor" to deliver a service.

I have gone under cover on occasion, and even have worn some disguises because I did not want to be hassled by some of these individuals.

We have an epidemic of quackery and health fraud being marketed through telemarketing and 800 call lines. All you need to do is have an unregistered telephone with an answering device on it, which I have, and you know that the sophistication of these groups is indeed pretty great.

They will talk to somebody on my answering device as easily as they will talk to me in person.

They also make great use of their knowledge of sales psychology and intimidation and threat. Where we start to get complaints in our organization is where those threats have gone a little too far.

But they are very brazen. I would not underestimate them at all. They are eventually going to harm the entire field of legitimate telemarketing if something is not done.

I am not going to go into all of the details, but I will give you a few examples. I think the Medigap insurance field is one. We have all seen the potential for harm there, especially when they start using nationally known television or movie stars or authority figures to help market it and list the 800 call line.

Vitamin and megavitamin supplements are a very profitable item. Within the last few days, we have had examples of people being sold hundreds of dollars worth of items.

Some of these things are harmless. But there is a type of telemarketing and quackery where people are offering cures for AIDS and for cancer. Indeed, we have one notorious quack that runs a unit across the border in Mexico, that trains people in the United States to call elderly people on the phone, offering cures for cancer.

I have personally purchased a bottle of T cells, the lymphocytes that you are supposed to have to protect you against AIDS. I have purchased those over a telephone line from an outfit in California.

There are weight loss schemes in great abundance that I don't need to go into detail about.

This is not just hurting people's pocketbooks. It is really harming their health.

I am especially concerned about the vulnerability of the elderly. I would like to dwell just for a minute on our responsibilities to the elderly.

They are, indeed, very vulnerable. Sixty percent of mail/phone/door-to-door fraud is perpetrated on the elderly.

There are reasons for this. The elderly are less mobile. They actually like to get telephone calls. They like to get a communication, whether it is in the mail or even through a catalogue. They do not do a very good job of comparison shopping. Many of them like the convenience of buying directly.

Also, 80 percent of them have chronic illnesses, and the rascals, the quacks and the frauds offer cures for these chronic illnesses, whether it is for cancer or arthritis or whatever. They also always have bargain prices, and most elderly know, if they are taking any legitimate medicine or take a number of legitimate medicines, that those are, indeed, very expensive.

They also promise cures where legitimate health services cannot promise a cure. They will zero in on some of the specific problems that the elderly have with impotence or with lost youth or maybe even in the insurance field, talking about their ability to stay independent and not become a financial burden.

If any of you really wants to hear a huckster, a real, live huckster, you ought to hear some of the sales pitches that these people have.

I just think we have a great responsibility to our elderly. They are much more trusting. I am especially concerned about the authority figures, such as movie stars or sports figures.

I hope in your study of telemarketing that you may look at the options of people somehow flagging their phone number to indicate that they do not want to receive a phone call from one of these organizations, such as we do with junk mail. Maybe there is some way that we could mark that so that privacy is respected.

I think also, giving the attorneys general expanded powers would be of great help, just because of the speed and the necessity to have an extended fight.

We are very, very frustrated by the growth of this industry. If you think telemarketing is a growth industry, I can tell you that so is quackery and health fraud. It is not just an economic burden.

I want to thank you for the opportunity to be here.

[The statement follows:]

STATEMENT OF DR. JOHN H. RENNER

Mr. Chairman, Committee Members. My name is John H. Renner. I am a family physician, and Director of Community Health for Trinity Lutheran Hospital, Kansas City, Missouri. I am a clinical professor of Family Medicine at the University of Missouri-Kansas City. I have been a health educator and consumer advocate for the past 25 years. In March of 1988, I co-chaired the federal Food and Drug Administration's National Conference Against Health Fraud, held in Kansas City.

The pending legislation this Committee is reviewing regarding telemarketing and fraudulent practices is vital. There is a clear need to regulate the present telemarketing industry, and to enforce vigorously such regulations, to protect the public from those elements that would profit through fraud.

One definition of telemarketing can be anyone who uses the telephone in the course of an average business day to conduct their business and uses or lists an 800 or toll-free number as their principal business number. Telemarketing involves not only receiving solicitation calls but also the ability to seek actively products or services through the access of the 800 or toll-free number system.

The sincere, legitimate companies that responsibly promote worthwhile items or services are in danger of being driven out of business by the actions of unscrupulous marketers of questionable or fraudulent items.

Under present conditions, telemarketing provides many opportunities for fraud. The abuse of telemarketing in this country has now taken us far beyond the old maxim, "Let the buyer beware". Telemarketing has become a highly sophisticated business. There are a number of individuals and firms that have extensively studied human psychology and have honed their sales techniques to manipulate deep-set psychological feelings for profit. The brazeness and sophistication of their techniques has intrigued and amazed even the most knowledgeable of physicians, and other health and scientific professionals.

I have personally been exposed to the telemarketing of such items as insurance for the elderly; diamond investments; real estate ventures; weight loss programs; diet aids; vitamin and megavitamin supplements; audio/visual tapes and books; contour chairs, adjustable beds and other health devices; charity fund solicitations; sales of lightbulbs and other items by "disabled" persons; and offers of cures for arthritis, AIDS, cancer, baldness, sexual impotency, and a host of other diseases and conditions.

I have seen talk shows and religious programs that feature a person promoting his or her cure for cancer or arthritis, or promoting a fad diet, and then seen a toll-free number provided to order the book, diet plan, or product or service.

I have seen celebrities, sports figures, and movie stars pitching a variety of products, services and treatments, all readily available through the 800 or toll-free number network.

As a health educator and consumer advocate, I am most concerned about the health offerings that these telemarketing firms make. I have received numerous complaints from all over the United States dealing with the purchase of questionable or fraudulent health care products which have proved to be of no benefit to the purchaser, or which have caused outright physical harm. Particularly vulnerable to health frauds, and especially to telemarketing schemes, are the elderly people of this country. They share, as a group, a number of characteristics that make them more vulnerable to fraud. Specifically (1) They are the victims of 60 percent of the country's fraud by mail, phone, and door-to-door solicitation. They are more often homebound and less mobile than the rest of society. They are less likely to comparison shop and more inclined to take advantage of the convenience of buying directly through the mail or by phone.

(2) Eighty percent of America's elderly have one or more chronic diseases. The marketers of health frauds, therefore, most often offer "easy", "miracle" or "breakthrough" cures, drugs, and other remedies specifically targeted to the elderly. They offer attractively priced items with claims of painless, effective results.

(3) The elderly may fall prey to fraudulent schemes that promote the ability to regain lost youth, independence, and self-sufficiency, all abilities the elderly cherish and have lost to their advancing years.

(4) The elderly take 25 percent of all prescription medicines in this country, and are more vulnerable to those schemes which offer a few pills or a single "wonder drug" in place of the six or seven pills the average elderly person takes.

(5) The elderly are more concerned about and conscious of their health. They can be motivated by manipulating their fears of having insufficient medical insurance, becoming a burden to their families, or losing all their possessions and self-sufficiency.

(6) In general, the elderly are more trusting than the rest of the regulation. They place more trust in authority figures and prominent people. They believe more readily that health-care advertising is strictly regulated and contains no misinformation. They are more likely to believe testimonial ads, having grown up in an era when remedies were passed down through the family or shared by neighbors.

Telemarketing firms seeking to defraud the elderly and other vulnerable individuals will play upon and enlarge existing fears, guilt feelings, and desires or needs. An example is the form of psychological harassment that can make someone feel extremely guilty, for example, that children are starving because they have failed to donate to a particular cause.

Based on the complaints I have listened to and investigated in the area of telemarketing and health fraud, I propose the following recommendations to this Committee to curb the widespread abuse of the telemarketing industry, and ensure the public's health and safety o It is essential to the government's ability to fight fraud to give the state attorneys general expanded powers under the federal trade rules legislation. They can be a powerful force in defeating telemarketing and other fraud perpetrators if they are given the proper tools.

It might be prudent to study whether it is feasible to mark directory 5elephone numbers indicating individuals who do not want telephone 8olicitation to invade their privacy - just as the Postal Service will not deliver so-called "junk mail" if the person fills out a form indicating they do not want to receive it. If such a project is not possible, then the current laws must be changed and future laws designed to protect the vulnerable and those wishing to keep their privacy intact.

Movie stars, sports figures, celebrities, and other dignitaries should be held accountable for the products, services, and other items they promote. These people often carry inflated credibility in the public's eye because they are perceived as "larger-than-life".

Ongoing efforts to educate the public, especially the elderly, to the detection and prevention of health fraud should be continued. Future programs should be dedicated to educating the public about the specific mechanisms behind telemarketing fraud.

Senator GORE. Thank you. Thanks to each one of you.

I am going to hold my questions down because we have run somewhat late. But let me ask a few questions before turning to Senator McCain.

Ms. King, in your written statement, you express concerns related to privacy, with the provision in S. 2326 that would permit the FTC to have access to mail covers for the purpose of tracking mail.

As I understand this provision, the FTC could not open the mail, but would have a record of the information printed on the outside of the mail—who it was sent to, where it came from, date and time, et cetera.

Law enforcement agencies dealing with crimes now have this authority. But the FTC, since it does not have criminal authority, is not entitled to request a mail cover under current regulations.

Specifically, what are your privacy concerns with this provision?

Ms. KING. Specifically, our concern was that the jurisdiction of the FTC was getting into a area that is not traditionally theirs, and, in order to look at that problem in depth, we would have to have a great deal more information about what government agencies are allowed to do such things. I presume that the Post Office can, in certain circumstances.

But I think it is a very serious additional authority of the FTC. We have grave reservations about incorporating that into this bill.

Senator GORE. Now, moving to another subject, let me just ask you this, generally. Does your group, the Consumers League, receive many complaints on telemarketing fraud?

Ms. KING. We have received some on occasion because of some of our media activities.

In the last year, in conjunction with some industries we have put out information to consumers about how to avoid telemarketing fraud. We have been rather prominently involved in media efforts.

In those cases, we hear from private parties.

Senator GORE. What kinds of items are they? What kinds of complaints?

Ms. KING. We heard a lot about travel, health fraud, and also overseas employment, which surprised us. We thought that might be a more isolated type of fraud. There are those areas.

Of course, we have heard substantially about investment fraud, but we had been directly involved in that issue. That was not surprising.

Those are the main areas that I can think of off-hand.

Senator GORE. You have testified that in your view it is imperative that the States have the authority to move against those persons preying on their citizens by way of telemarketing fraud.

Why do you feel that State laws are insufficient in this regard?

Ms. KING. The State laws are insufficient because, for one thing, they are far from uniform. Number two is the difficulty that States have regarding the ease in crossing State lines.

I have been involved in this issue one way or the other for six years, and this has been a chronic, constant complaint, that these people can move so fast.

We think that H.R. 4101 addresses that problem through the authority to sue in the Federal courts and giving the attorneys general the capacity to move very quickly.

The FTC simply is a slower mechanism for dealing with the problem.

Senator GORE. Commissioner Calvani earlier said he liked the provision in S. 2326 allowing the FTC to delay notice to consumers that it has obtained access to their financial records in order to avoid destruction or dissipation of assets. And yet, the National Consumers League has some objection to that.

Could you spell out why you are concerned about that.

Ms. KING. It is a similar objection to the privacy objection that we expressed, about the tracking of mail covers.

I would say this is not a substantial reservation if it is something we could look at more closely and could see that the reason for it was very clear.

As we understand now, the attorneys general can do this anyway. Should that be the case and the reason be sound, we can understand it.

But, again, we had reservations about giving the FTC this authority.

Senator GORE. You stated support for a study of the life care, the home industry.

I might just note that this year's FTC bill, which has been in conference committee in one form or another for about eight years now, I guess, has a study on Medigap insurance, agreed to on the Senate floor. I think there is widespread agreement on that. I would hope that we somehow could get that passed.

I might say, for the record, that we have not given up on the FTC bill this year. We are really hoping that we can pass one.

But it has been tough for the last several years.

Dr. Renner, you state that you support giving the State attorneys general expanded powers.

Is that correct, and why is that?

Dr. RENNER. Every week I get a report from an attorney general's office where they brought action against something that is a violation of either FDA or State laws. I just know how assertive, aggressive, and knowledgeable they are.

I just think that this would give the attorneys general very much needed expanded legal service to the public, especially. They can move against products right now rather easily. But some of these other things in telemarketing involve health services which are legally more complicated.

I think that those legal expansions would be very helpful, and I have seen their track record of how they delivered on their procedures by not taking frivolous action.

Senator GORE. Thank you.

I am going to submit questions to you in writing, Mr. Levering, and I appreciate your testimony as well.

I want to recognize my colleague, now, Senator McCain.

Senator McCAIN. Thank you, Mr. Chairman.

I would like to state to you, Mr. Chairman, that I think this has been a very valuable hearing. I think we have a lot of good information, and perhaps we can work out some agreements so that we can move forward on this.

Senator GORE. I certainly hope so.

Senator McCAIN. Ms. King, thank you for your testimony and especially for all that you and the National Consumers League have done on this issue. We are very appreciative.

I have been told that it is sometimes difficult to locate and get victims to come forward and testify against con artists.

Are you aware of this problem, that they are embarrassed and don't know who to go to, et cetera?

Ms. KING. Yes.

We were co-producers of tapes in this past year and found it difficulty even then, when we had names of people, to get them to come forward.

I think the reason is obvious. After someone has been victimized, they may feel stupid. They may be embarrassed, even with their own families—especially, again, the elderly would come into this category.

Senator McCAIN. Also, in addition to that, they don't want the hassle perhaps and they figure it probably won't happen again.

Ms. KING. In fact, someone from AARP pointed out last week that older people sometimes feel like they are relinquishing their independence if they go to an agency, even go to a lawyer for help. So I think that is a very clear problem here.

Senator McCAIN. Clearly, Dr. Renner, from your gestures you agree with what Ms. King has just said.

Dr. RENNER. Absolutely.

We have tried over and over again to get people to file complaints and told them exactly what steps to take and what organizations to get in touch with. When we follow up, we find out they are just too embarrassed.

Senator McCAIN. Thank you.

Let me point out, Ms. King, that that was one of the primary reasons why we included in my legislation the ability of the FTC to locate victims, by tracking the destination of the mail sent by suspected quacks and con artists. I hope that we can resolve in a very specific fashion the concerns you had on that aspect of the bill, because there certainly is not intention to violate anyone's privacy. I hope we can perhaps work together in the future on that.

Ms. KING. We certainly are willing to.

Senator McCAIN. Thank you.

Also, Ms. King, let me ask this.

We have talked about telemarketing fraud, but you also mentioned that there are other forms of fraud that do not involve telemarketing, much of which you have been involved in.

Should we be addressing those as well?

Ms. KING. I would think so.

I know we have to separate it out and I know your bill deals specifically with quackery. We are very interested in that problem and only some part of it results from telemarketing.

Senator McCAIN. Thank you.

Dr. Renner, we have been the recipient, I am happy to say, of some of the information that you have in our work on this legislation, and we are very grateful for it.

We are nearing the end of our period here today. Could you describe some of this, particularly the Toftness detector. Would you describe that one for the record.

Dr. RENNER. That was a gadget that was sold. I think there were 2,500 of them sold. It was supposed to help detect the appropriate amount of radiation.

It was just a pure, quack device that was actually perpetrated on a group of chiropractors. They, in turn, then would turn around and sell the service to their customers.

They had research papers on it. They had everything. It was a very sophisticated scam.

We included that because all of this is not simple at first glance to detect. That was something that was backed up with publication of papers. It was an extremely profitable thing. It cost only a few pennies to make but sold for $2,500.

Senator McCAIN. For $2,500, and they sold 2,500 of them?

Dr. RENNER. Yes. That's just the tip of the iceberg.

The other thing I am convinced of is that we only see a small part of the health fraud and quackery that is perpetrated in this country. Most of it goes absolutely unreported, and what we are bringing to you is just a small fraction of what is really going on out there.

If you start looking for it and digging for it, as we have in one or two cases, it is pretty startling.

Senator McCAIN. I think we might have mentioned in our communication to you regarding the Toftness detector. There is an Arizona citizen who is now paralyzed as a result of a chiropractor who used this and failed to detect a spinal tumor.

Finally, I have just one other question for Ms. King and Dr. Renner.

Mr. Levering, we appreciate very much your testimony. I just have no questions for you.

Why in the world would people risk their good names, individuals that we admire and respect, who have been in the entertainment and athletic worlds and others, by lending their names to these fraudulent schemes?

Ms. KING. I think I originally assumed that they did not know what they were selling. I am no sure it is so innocent, because I understand some of these people have been notified, especially in the Medigap area.

I cannot explain it because from my point of view, it is immoral to be selling these products once people understand that some of them are fraudulent, truly fraudulent in nature.

I do not understand it.

Senator GORE. Well, they're getting a lot of money, aren't they?

Senator MCCAIN. I know they are getting a lot of money, but most of these people are already rich and they have good names in our society.

Dr. RENNER. It is ego. It is being in front of the public again. It is money.

Sometimes it has an anti-establishment quality to it.

Some of them ought to be required to swallow some of the pills that they are selling themselves.

Senator MCCAIN. On that note, I thank you, Mr. Chairman, and I thank the panel very much.

Senator GORE. I recently saw a very famous actor attempt to sell a device that would shoot down all incoming Soviet missiles for only a trillion dollars.

I had the same kind of bewilderment there.

Let me just say before I provoke an equal time requirement here that, with regard to the scope of the two bills before us, I am very sympathetic to the idea of a larger, more expansive bill.

I want the record to show that the short period of time remaining in this legislative session, coupled with the action already taken by the House of Representatives and the anticipated opposition to each additional provision that is added to a larger bill, those concerns are the main ones why my own personal view is that in this legislative session of Congress, another 20-some-odd days, the odds of success are probably greater for a bill with a narrower scope.

But I want to join my colleague in also expressing a desire to work together to see Republicans and Democrats on the committee come together in support of a bill that can pass, that we can get out of conference in the short time remaining.

I want to thank all of the witnesses that we have had here today.

This hearing is adjourned.

[Whereupon, at 5:01 p.m., the subcommittee adjourned.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

STATEMENT OF THE ASSOCIATION OF NATIONAL ADVERTISERS, INC.

Mr. Chairman, we appreciate the opportunity to provide testimony on the important issue of telemarketing fraud. As you know, the Association of National Advertisers, Inc. (A.N.A.), is dedicated to representing the interests of national advertisers. Our membership includes almost 300 companies, with over 2,000 subsidiaries and divisions located throughout the United States. A.N.A.'s Members collectively account for over two-thirds of all national and regional advertisers expenditures in this country.

In general, A.N.A. is not primarily concerned with telemarketing issues. But the three telemarketing bills presently pending before this Subcommittee, S. 2213, S. 2326, and H.R. 4101, are so broad and open-ended in scope that they inevitably will have a significant impact on the advertising community. A.N.A. also is deeply concerned about the effect these bills will have on the relationship between federal and state governments in regard to the regulation of interstate commerce.

A.N.A. believes strongly that telemarketing fraud is a major national issue which must be addressed. The Federal Trade Commission (F.T.C.) received approximately 3,100 complaints concerning telemarketing fraud in 1987, and this number is likely to be surpassed in 1988. We commend the Consumer Subcommittee for spotlighting this critical problem and strongly support the goal of strengthening governmental efforts to eliminate telemarketing fraud.

As a general principle, A.N.A. believes that in regulating activities which directly impact interstate commerce, the federal government must take the lead role. Federal regulation of interstate commerce is the most effective means to assure a fair and efficient national marketplace. We believe federal coordination is particularly crucial with regard to activities in the complex and diverse telemarketing area, a $100-billion industry which affects citizens in virtually every region of this country.

In recent years the Federal Trade Commission has been working actively with state attorneys general to combat telemarketing fraud. As the Chairman of this Subcommittee, Senator Gore, stated on the Senate floor on March 24, 1988, "The F.T.C. is *uniquely* situated to address these issues, with authority to conduct investigations, provide consumer redress and seek injunctive relief." [emphasis added] We believe the F.T.C. has shown itself to be a willing and aggressive policeman in the telemarketing area.

H.R. 4101 and S. 2213, however, give every state attorney general and "any other official of a state vested under state law with the authority to enforce state consumer protection laws" vast new powers to bring civil actions in the federal district courts in the telemarketing area. These suits could be commenced to enforce rules promulgated under the F.T.C. Act *or* to stop a telemarketer who is perceived to be engaged in a "fraudulent or dishonest act or practice." A.N.A. has a number of serious concerns with these provisions.

First, A.N.A. believes that permitting the state attorneys general to enforce their own fraud statutes regarding telemarketing in federal district court will inevitably lead to fragmentation of national enforcement policy, the loss of Congressional control over the regulation of an important aspect of interstate commerce and the development of inconsistent and conflicting judicial decisions concerning telemarketing fraud. To allow the state attorneys general and other state officials to bring federal action against telemarketing schemes under their own state fraud statutes is an enormously broad delegation of power. State fraud statutes are infinitely expandable and outside of any federal control. Therefore, the states under both H.R. 4101 and S. 2213 potentially will have more extensive powers than the F.T.C. to combat fraudulent interstate telemarketing schemes.

If Congress believes more needs to be done to combat telemarketing fraud nationwide, it certainly has readily available vehicles with which to strengthen existing federal efforts. Legislation to reauthorize the F.T.C. has sat in limbo since 1982. Congress has the ability through the F.T.C. authorization bill or through other independent legislation to increase immediately the funding of the F.T.C. and require that a specific portion of that additional funding be allocated to investigate telemarketing fraud. Congress also can demand periodic reports by the F.T.C. on its progress in combating telemarketing schemes and on the F.T.C.'s efforts to coordinate and cooperate with state and private initiatives to counteract telemarketing fraud. This is certainly the most direct method by which the Congress can help combat telemarketing fraud without abdicating its interstate commerce responsibilities to the state attorneys general. Unfortunately, H.R. 4101 and S. 2213 tend to ignore the need to support and enhance the F.T.C.'s efforts in favor of shifting regulatory authority and power to the states.

A.N.A. recognizes that the states have an important role to play in the war against telemarketing fraud. Often state officials have important information that can be of use to federal authorities as well as other states. The F.T.C. already has developed extensive cooperative efforts in the telemarketing area with the state attorneys general. But, A.N.A. believes that if we are to have a national, uniform, coordinated policy in the telemarketing area, a federal agency must control the process.

If, after providing the F.T.C. with increased resources and direction concerning the telemarketing issue, Congress still finds that the states need to be given an enhanced role in the process, then the F.T.C. could be empowered to "deputize" state attorneys general to assist them in specific and limited telemarketing enforcement actions. The deputization of state officials by the federal government has proven successful in other areas and permits the federal government to retain control while obtaining additional assistance from the states. Certainly, this more coordinated national approach should be tried and fully tested before any thought is given to providing the states an open-ended and uncoordinated delegation of responsibility in the telemarketing field.

H.R. 4101 and S. 2213 not only delegate federal enforcement authority to the state attorneys general in the telemarketing area but give "any other official of a state vested under state law with the authority to enforce state consumer protection laws" the power to bring actions in federal district court. This undefined group of state officials could include the state police, state securities departments, state alcohol commissions, various state licensing boards, including those with jurisdiction over lawyers, cosmetologists, doctors, architects, etc., state health departments as well as numerous other state officials including low-level functionaries. Certainly all these state officials, it can be argued, are vested with "authority to enforce state consumer protection laws." A.N.A. believes such an undefined delegation of enforcement power can only cause confusion and prove counterproductive.

Further, S. 2213 and H.R. 4101 only require that the state attorneys general and other state officials notify the F.T.C. regarding their plans to commence a civil action in the telemarketing area. Other federal entities, which may have a need to know of such activity, are not required to be notified. Thus the Department of Justice, the Securities and Exchange Commission, the Federal Communications Commission, the Department of Treasury, The Department of Transportation, and the Food and Drug Administration, to name just a few examples, will not be required to be given timely notice of a state action which may directly impact them. Surely these important issues need to be thought through and resolved before any action is taken on this legislation.

In addition, Congress should give careful attention to the definition of "telemarketing" contained in all three bills. As now defined, telemarketing means "the use of a telephone in the ordinary course of business to communicate with a person an offer for sale or to complete a sale of a product or service." Under this definition, use of a telephone to complete a sale could bring the transaction within the boundaries of the telemarketing law. As such, many transactions for auto service repairs, Pizza parlor and other home delivery orders, airline reservations and ticketing, catalog ordering, flower delivery orders, and stock brokerage transactions could all be subject to the provisions of the telemarketing law.

If this legislation were to pass in its current form, the inevitable onslaught of state and private federal telemarketing actions will place a heavy burden on an already overworked federal judicial system. The multitude of potential new federal suits could result in inconsistent federal court interpretations and, unfortunately for American consumers and business, uniform national telemarketing enforcement will be placed in serious jeopardy.

Finally, A.N.A. is concerned about the extremely tight time limits and limited procedural safeguards required in H.R. 4101 and S. 2213 for the mandated F.T.C. telemarketing rulemaking. To develop a rule in the complex and diverse telemarketing area that will adequately regulate fraudulent telemarketers without unduly burdening honest businesses will be extremely difficult under the best of circumstances. By compressing the rulemaking, various affected segments of the industry will not be given adequate time to be heard fully. This is likely to engender rules which burden honest telemarketers while concurrently increasing the danger that loopholes will be created for the unscrupulous. The rulemaking required by this legislation encompasses enormous segments of industry. It will affect the rights of numerous consumers and businesses. This is precisely the type of circumstance that led the Congress to provide the F.T.C. with trade regulation rulemaking powers, and they should be used if a rule is to be mandated in the telemarketing area.

We believe that carefuly crafted telemarketing legislation would be a major step in providing protection for consumers and honest businessmen and help maintain a more honest marketplace. A.N.A. stands ready to provide whatever assistance we can to the Subcommittee and its staff in strengthening and refining the important telemarketing legislation presently pending before the Senate Commerce Committee.

Thank you.

STATEMENT OF THE ATTORNEYS GENERAL OF THE STATES OF NEW MEXICO AND UTAH

The Attorney General of the State of New Mexico, Hal Stratton, and the Attorney General of the State of Utah, David L. Wilkinson, submit this statement to the Consumer Subcommittee of the United States Senate Commerce, Science and Transportation Committee in support of Senate Bill 2326, which would improve the Federal Trade Commission's ability to deal with telemarketing fraud.

In both New Mexico and Utah, the Office of the Attorney General is the primary consumer advocate for the state's citizens. For instance, in New Mexico the Office of the Attorney General is the only governmental agency that accepts and processes complaints from consumers. In Utah, while there is a separate state division of consumer protection, the Attorney General represents the division, and brings all consumer protection actions that are filed in the name of the state.

The New Mexico legislature has assisted the attorney general's consumer protection efforts by enacting various laws that prohibit fraudulent and illegal activity directed against consumers. Those laws include the Anti-Trust Act,[1] the Unfair Practices Act,[2] the Pyramid Promotional Schemes Act,[3] the Price Discrimination Act,[4] the False Advertising Act,[5] the Motor Vehicle Quality Assurance Act[6] and the Charitable Organizations and Solicitations Act.[7] Over the past two years the New Mexico legislature has adopted amendments that the Attorney General has recommended to strengthen the Unfair Practices Act and the Pyramid Promotional Schemes Act. The New Mexico Attorney General's Consumer Division uses these statutes and general common law concepts to assist consumers in protecting themselves. We particularly rely upon the Unfair Practices Act as a comprehensive tool to remedy and prevent unfair, deceptive and unconscionable trade practices directed at consumers, including telemarketing fraud.

Telemarketing fraud has become one of the more troublesome and common forms of consumer fraud in recent years. Although we do not have any definite figures, we can say that our respective consumer divisions are receiving more and more telemarketing fraud complaints.

Those engaging in telemarketing fraud appear to single out senior citizens for their unscrupulous schemes. Senior citizens frequently are home much of the day, and therefore receive more phone calls and solicitations than the average citizen. They also frequently have accumulated considerable savings during the course of their lives. Both factors make them good targets for unscrupulous and fraudulent telemarketers. Because they very well may be exposed to more fraud, we naturally have a high degree of concern for senior citizens.

In light of the escalation of telemarketing fraud around the country, the New Mexico Attorney General is participating in the Federal Trade Commission's automated data bank on telemarketing fraud program. This shared data enables us to identify serious violators and facilitates evidence of telemarketing fraud. We have joined with a number of other states and are attempting to coordinate with the National Association of Attorneys General, the F.T.C. and other law enforcement agencies around the country in this project.

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[1] Sections 57-1-1 to 57-1-19 NMSA 1978.

[2] Sections 57-12-1 to 57-12-15 NMSA 1978.

[3] Sections 57-13-1 to 57-13-18 NMSA 1978.

[4] Sections 57-14-1 to 57-14-9 NMSA 1978.

[5] Sections 57-15-1 to 57-15-10 NMSA 1978.

[6] Sections 57-16A-1 to 57-16A-9 NMSA 1978.

[7] Sections 57-22-1 to 57-22-11 NMSA 1978. Utah has similar consumer protection legislation, but in the interest of brevity we do not list it here.

However, telemarketing fraud has become so pervasive that we believe Congress must give the F.T.C. additional weapons to combat telemarketing fraud schemes. That is why we support Senator McCain's Senate Bill 2326. It substantially improves the Federal Trade Commission Act and the F.T.C.'s ability to enforce the Act against telemarketing fraud.

We understand that currently three bills are pending before the Consumer Subcommittee on this subject: Senate Bill 2326, Senate Bill 2213 and House Bill 4101 (companion to S. 2213). We believe that Senate Bill 2326 will be the most useful and effective piece of legislation to assist the F.T.C. in fighting telemarketing fraud. We will not discuss the relative merits of the substantive changes to the Act that these bills make. We are quite sure that Senator McCain and other witnesses before the Subcommittee will adequately cover these changes. We would, however, like to address one aspect of the bill that we believe will greatly affect our offices and the offices of other state and local governmental attorneys around the country. Senate Bill 2326 would allow the F.T.C. to appoint state attorneys general to assist in enforcing rules that it promulgates. Senate Bill 2213 and House Bill 4101 would authorize states, in their discretion, to bring their own civil actions against fraudulent telemarketers under Section 19 of the Federal Trade Commission Act, without F.T.C. approval or authorization. This provision would allow all of the attorneys general of the fifty states and five territories—and potentially many thousands of other local district, county and other governmental attorneys—to bring actions under the Federal Trade Commission Act. We believe that the approach suggested in Senator McCain's bill is superior. We will briefly discuss our reasons for this position.

Both of us strongly support the concept of federalism, in particular the broad rights of state governments as contemplated by the Constitution. We believe that our job as state attorneys general is primarily to enforce state law within our respective jurisdictions. This does not mean that we do not or will not assist and coordinate with federal authorities in criminal and civil investigations and enforcement actions under federal law. On the other hand, we also believe that federalism dictates that federal agencies should be primary instruments to carry out the national policy that Congress establishes. Specifically, the Federal Trade Commission should direct enforcement of the Federal Trade Commission Act. If the F.T.C. determines that it needs help (or when we can persuade them that they need us), it can request the assistance of state attorneys general.

If each state attorney general is allowed to enforce the Federal Trade Commission Act at his discretion, the provisions of that Act may supplant state law covering the same subject matter. Practically speaking, because the Federal Trade Commission Act is more pervasive and oftentimes more specific, state attorneys general very well may end up enforcing that act rather than the fifty states' laws. State consumer protection laws will be unenforced. We believe that if our state legislatures wanted us to act under such a statute as the Federal Trade Commission Act within our jurisdictions, they would have adopted such legislation and made it the law of our states.

The provision in Senate Bill 2213 and House Bill 4101 that would allow fifty-five state and territorial enforcement policies also effectively would take the national policy of telemarketing fraud enforcement out of the hands of the Federal Trade Commission. Each attorney general would not be subject to any control or direction by the F.T.C. and could determine, without any input by the F.T.C., his or her states' policy for enforcing federal law. This most likely would result in many inconsistencies, not only in enforcement of the Act within each state, but also in court decisions and positions taken by government attorneys across the country.

In conclusion, Senate Bill 2326 would establish a cooperative relationship between the states' attorneys and the attorneys for the F.T.C. We believe that the joint coordinated efforts that Senate Bill 2326 contemplates would be most effective in combating telemarketing fraud around the country. The Attorneys General of New Mexico and Utah therefore would urge the Committee to adopt Senate Bill 2326 to assist all of us who are interested in curtailing telemarketing fraud.

STATEMENT OF NEAL F. HARTIGAN, ATTORNEY GENERAL, STATE OF ILLINOIS

More Americans than ever before are shopping at home through the use of their telephone. In particular, many senior citizens find it more convenient, or their health necessitates that they utilize the telephone for their shopping needs. In recent years however, the state Attorneys General have witnessed the rapid acceleration of fraudulent telemarketing sales as scam operators cash in on this shift in consumer buying habits.

The telephone has been used to peddle a wide variety of goods and services ranging from phony investments to substandard office equipment and supplies. More sophisticated technology and the ease with which transactions can be charged to a credit card have enabled fraudulent telemarketers to steal from citizens nationwide. Scam operators are able to take in large amounts of money in a short time and then disappear, leaving consumers with little recourse. In fact, it is estimated by law enforcement officials that Americans are defrauded out of at least one billion dollars a year.

The victims of these scams represent a cross-section of Americans—from senior citizens who have recently received insurance money and are seeking advice on how and where to invest it, to operators of small businesses who are deceived into purchasing unnecessary or substandard office supplies. Nearly every home in this country has a telephone and is a potential target for fraudulent telemarketers. Telemarketers may operate with live operators or with automatic dialing devices. Either way, the intrusion into homes is almost constant.

Once a scam operator has a consumer on the line, the high pressure sales pitch begins. Consumers are induced to buy a wide range of phony products including vacation packages, office supplies and oil and gas leases. Misrepresentations run rampant through the fast-paced presentations. Consumers are urged to "act immediately," to take advantage of "once in a lifetime deals" and to give out credit card numbers to insure their order is placed in time.

Telemarketing fraud represents a unique and difficult enforcement problem for state Attorneys General. A fraudulent telemarketer merely sets up a "boilerroom" operation consisting of a bank of phones, phone operators and lists of potential consumer victims. The operation can be easily dismantled when discovered by law enforcement officials.

Phony telemarketers then begin solicitation of consumers nationwide, while avoiding marketing in their own state in order to hide from local authorities. Scam operations change names and schemes frequently and, if close to discovery by law enforcement officials, they simply jump across state lines and begin anew.

Under current consumer protection laws, a state Attorney General is only empowered to obtain an injunction in his/her own state, leaving the scam operators free to solicit in 49 other states. Furthermore, once the injunction is obtained, recovery of monies in these cases is rare due to distant location of telemarketers in other state jurisdictions and the ease with which they can elude a state's grasp.

Over the last two years, the National Association of Attorneys General and the Federal Trade Commission have focused on telemarketing fraud and have fashioned a unique cooperative enforcement strategy to fight the problem. The cooperative effort incorporates not only the state Attorneys General and the Federal Trade Commission, but the Department of Justice, the Secret Service, and the Postal Inspectors as well as a number of private businesses and organizations representing legitimate direct marketing companies.

First, state and federal law enforcement agencies cooperativley targeted the most egregious fraudulent telemarketing operations. Then over seventy lawsuits were filed in early 1987 by twenty-two states and the Federal Trade Commission. Dozens of additional cases have followed.

Second, the coordinated attach on telemarketing fraud has culminated in the creation of a computer data bank located with the Federal Trade Commisson (FTC) which catalogs fraudulent operations and their locations, the amounts of money taken, the numbers of victims, and active investigations as well as existing law enforcement actions across the country. This data bank makes computerized information available to any participating agency so that it can effectively proceed with prosecution. It simultaneously reduces duplicative efforts, builds upon existing work done by others and increases the effectiveness of law enforcement efforts.

Senator Gore's proposed telemarketing bill, Senate Bill 2213, now before this committee would amend the Federal Trade Commission Act, Section 19, to permit state Attorneys General to bring actions in federal district court against persons who commit a fraudulent or dishonest act involving the use of the telephone. Federal court jurisdiction carries with it the benefit of nationwide service of process and the ability to secure the assets of the defendant which are located in another state.

In addition, the legislation would enable a state Attorneys General to bring a single proceeding in federal court to stop the operations of a fraudulent telemarketer soliciting in a number of states. Under Senate Bill 2213, wasteful use of state and federal resources would be eliminated as the states would no longer have to file fifty separate but virtually identical actions to halt a single telemarketer. For example, in August 1984, North Carolina sued Mytel International claiming that its telemarketing sales violated North Carolina's Consumer Fraud Act. In June 1985, Mytel entered into a consent judgment with North Carolina. In January 1987, Illinois sued Mytel, alleging that its telemarketing sales violated the Illinois Consumer Fraud Act. In June 1987, Mytel entered into a consent judgment with Illinois. In October 1987 the Federal Trade Commission sued Mytel also.

I also am aware that Senator McCain has introduced Senate Bill 2213 which would increase the power of the Federal Trade Commission in the area of telemarketing fraud and allow for the Commission to deputize State Attorneys General to enforce FTC rules. While Senator McCains' bill bolsters the Commission's authority in the telemarketing fraud area, it gives the states no enforcement powers unless each Attorney General is specifically deputized by the FTC. Senator Gore's bill, Senate Bill 2213, is preferable to State Attorneys General as it would provide that authority be vested in State Attorneys General to enforce the provisions of this proposed telemarketing law.

Senate Bill 2213 would allow states to bring national enforcement actions against the full spectrum of scams ranging from magazine sales schemes to vacation scams, from bogus contests to the rapidly growing health fraud area. This bill well serves the law enforcement interests of quick prosecution, effective use of state and federal resources, and appropriate use of court time by granting a state attorney general prosecuting a phony telemarketing operation a national injunction and redress in federal court.

STATEMENT OF JUDGE WILLIAM W. SCHWARZER ON BEHALF OF THE JUDICIAL CONFERENCE OF THE UNITED STATES

Mr. Chairman and members of the Subcommittee, I am William W. Schwarzer, United States District Judge for the Northern District of California and Chairman of the Committee on Federal-State Jurisdiction of the Judicial Conference of the United States. I appreciate the opportunity to submit a written statement on behalf of the Judicial Conference of the United States for the record on pending telemarketing legislation. The Judicial Conference is the policymaking body of the Federal Judiciary. One of the functions of the Committee on Federal-State Jurisdiction is to make recommendations to the Judicial Conference concerning legislation relating to federal jurisdiction and federal-state relations and, on behalf of the Judicial Conference, to provide the Congress with any insights on the legislation from the perspective of the judiciary.

This Subcommittee is considering three bills intended to strengthen the Federal response to telemarketing fraud in a number of ways—S. 2213, S. 2326, and H.R. 4101. Two of these bills—S. 2213 and H.R. 4101 (as passed by the House)—contain provisions to create new civil causes of action in the Federal courts for fraudulent telemarketing activities.

The purpose of my remarks is to address the potential impact of this legislation on the Federal courts and on their ability to meet the already heavy demands on their limited resources.

To put it into a nutshell, these bills would give Federal courts jurisdiction over all suits brought by individuals or State attorneys general for fraud in any sales transaction in which the telephone was used. The House bill would limit jurisdiction to claims exceeding $10,000.

It is immediately apparent that these bills go far beyond what is generally considered telemarketing, i.e., an organized interstate campaign to sell particular products in large volume. These bills would allow a disgruntled purchaser of a used car, for example, or a residence, or a home repair service, to sue in Federal court.

More than that, the bills would positively encourage the bringing of such cases in Federal court because they would allow the plaintiffs to recover attorney fees and expert witness fees, something they ordinarily cannot do in State court.

The question for Congress to ask is whether a justification has been shown to take most of the fraud cases involving use of a telephone out of the State courts and move them into the Federal courts. I am not aware of any evidence that suggests that State courts do not provide adequate remedies.

If the thought is that this legislation is needed to deal with significant fraudulent schemes in interstate commerce, the answer is that an adequate Federal remedy is already on the books in the Civil RICO Act (18 U.S.C. § 1964(c)). That Act provides civil remedies, in addition to criminal penalties, against persons engaged in a pattern of racketeering, which includes carrying out fraudulent schemes. It also allows plaintiffs to recover attorneys fees.

The wide sweep of RICO, which now allows State and local common law fraud actions to be moved from State to Federal courts, has led to questions whether it does not go too far. But the much wider sweep of these bills would generate a volume of litigation that I believe would dwarf the case volume under RICO.

One indication of the volume of cases that might be brought in the Federal courts under these bills is the volume of diversity of citizenship cases filed in those courts. These cases also have a jurisdictional minimum of $10,000 but they require in addition that all plaintiffs and all defendants be citizens of different states. Currently these cases are being filed at a rate of approximately 70,000 per year—one-quarter of all civil filings.

These bills do not even require diversity of citizenship. Jurisdiction would exist of any dispute over any kind of sales transction in which the telephone was used and a claim of fraud is made. It is not difficult for a plaintiff to make such a claim to get into Federal court and gain the benefits of these bills, including the right to attorneys fees.

In short, it is entirely possible that these bills, if enacted, could eventually increase the Federal courts' case load by as much as 50,000 cases or more per year—some ten to twenty per cent.

The Federal courts should, of course, serve the needs of the public. But there are now heavy demands on the courts—to further the war on drugs, to enforce civil rights, to help protect the environment, and to carry out the mandate of Congress in many other areas. The courts are badly extended to meet these many demands with very limited resources. To add the burdens of this legislation would take a substantial toll on the ability of the Federal courts to do the essential work they have been doing.

I appreciate the opportunity to present these observations to the Subcommittee on behalf of the Judicial Conference. I hope they will be helpful to members of the Committee and the Senate in considering this legislation.

STATEMENT OF BARRY A. FISHER ON BEHALF OF THE CALIFORNIA COUNCIL OF THE BLIND

This testimony is submitted on behalf of the California Council of the Blind. Founded in October, 1934, in Fresno, California, the Council is the largest organization of blind and visually impaired persons in the United States, with forty-five local chapters and some three thousand members. All of its officers are blind people. It is the California affiliate of the American Council of the Blind, which itself is the largest national organization of the blind and visually impaired. The goal of the California Council of the blind is to attain full independence, equality of opportunity, and social acceptance for blind people. It is an advocacy organization, which, in its half-century of existance, has pioneered and promoted many avenues of vocational and avocational achievement. It publishes a quarterly journal, *The Blind Californian,* which appears in Braille, recorded and large print versions; maintains an extensive scholarship program for blind people; provides advisory, counseling and referral services, including a toll-free referral number; organizes educational conferences and seminars; assists with employment and job placement; and counsults with public and private agencies on behalf of the blind.

The California Council of the Blind is dependent upon contributions from members of the public, and it particularly relies upon professional fundraising and consulting companies that go to the public on its behalf. Between sixty and ninety percent of its annual income is derived from campaigns carried out by such firms. Many of the fund-raising firms engage in telephone solicitations in which contributions are solicited in exchange for tickets to live theatrical performances. The Council is thus concerned about the potential reach of S. 2213 and the other bills before the subcommittee.

As presently drafted, the bill might be interpreted to encompass telephone solicitations by religous and charitable organizations, an application not consistent with the purpose of the legislation as I understand it. Over the past fifteen years, I have represented not only the California Council, but a number of religious and charitable organizations, many of which rely on fund-raising methods like those used by the Council. Additionally, I am the chairperson of the American Bar Association Subcommittee on Religious Freedom.

In preparing this testimony, I have examined three bills, S. 2213, H.R. 4101, and S. 2326. The first two, S. 2213 and H.R. 4101, although somewhat different, both pertain specifically to telemarketing, and thus raise the greatest concern for charitable organizations that raises funds through telephone solicitations. S. 2326, which pertains to consumer fraud more generally, contains one subsection regulating telemarketing. The following comments are directed specifically to S. 2213, but would pertain as well to closely analogus provisions of the other two bills.

S. 2213 defines telemarketing as "the use of a telephone in the ordinary course of business to communicate with a person and offer for sale or to complete a sale of product or service." While the bill was apparently not designed to cover religious or charitable solicitations, it might be stretched to reach such activities since those organizations sometimes sell tickets to benefit shows, tangible goods such as pencils or return address labels, decorative seals, advertising space and the like in connection with their solicitations. To avoid chilling the first amendment rights of religious and chartiable organizations, however, the bill may easily be amended to avoid any possible confusion, so as to provide:

> "For purposes of this section a religious or charitable organization, or a person, partnership or corporation soliciting on behalf of a religious or charitable organization, is not a person, partnership or corporation which engages in telemarketing."

This exemption for religious and charitable solicitation is compelled by recent Supreme Court decisions holding that charitable solicitations are fully protected by the first amendment. *Village of Schaumburg* v. *Citizens for a Better Environment*, 444 U.S. 620, 100 S. Ct. 826 (1980); *Secretary of State* v. *Joseph H. Munson, Co.*, 467 U.S. 947, 104 S. Ct. 2839 (1984); *Riley* v. *National Federation of the Blind of N.C.*, 108 S. Ct. 2667 (1988).

In *Schaumburg* the Court invalidated a local ordinance requiring charitable solicitors to use, for charitable purposes, 75 percent of the funds solicited. The village justified its ordinance arguing that charitable solicitation is akin to a business proposition and therefore constitutes merely commercial speech. The court rejected that approach and determined that charitable solicitations are so intertwined with speech that they are entitled to the protection of the first amendment:

> "Prior authorities, therefore, clearly establish that charitable appeals for funds, on the street or door to door, involve a variety of speech interests—communication of information, the dissemination and propagation of views and ideas, and the advocacy of causes—that are within the protection of the First Amendment. Soliciting financial support is undoubtedly subject to reasonable regulation but the latter must be undertaken with due regard for the reality that solicitation is characteristically intertwined with informative and perhaps persuasive speech seeking support for particular causes or for particular views on economic, political, or social issues, and for the reality that without solicitation the flow of such information and advocacy would likely cease." 444 U.S. at 632, 100 S. Ct. at 833.

Munson and *Riley* elaborated on the *Schaumburg* theme emphasizing that charitable solicitations were "inextricably interwined with * * * fully protected speech." *Riley, supra*, 108 S. Ct. at 2677. *Riley* also emphasized that protected speech would necessarily be chilled if a fundraiser for a charitable organization "must bear the cost of litigation and the risk of mistaken address finding by the fact finder." *Id.* at 2676.

Two sections of S. 2213 converge to make the bill unconstitutional as applied to solicitations by religious and charitable organizations.

First the bill is overbroad and impermissibly vague. Section 2(d) provides:

> "A person, partnership, or corporation which engages in telemarketing may not engage in any conduct the natural consequence of which is to harrass, oppress, or abuse any person in connection with the telemarketing. A person, partnership or corporation who engages in such conduct shall be considered to have engaged in an unfair or deceptive act or practice in or affecting commerce."

The standard, "conduct the natural consequences of which is to harrass, oppress or abuse any person," is similar to the standard condemned in *Coates* v. *Cincinnati*, 402 U.S. 611 (1971). (Conduct "annoying to persons passing by.") The Court found the law unconstitutionally vague saying:

> "Conduct that annoys some people does not annoy others. Thus, the ordinance is vague, not in the sense that it requires a person to conform his conduct to an impercise but comprehensible normative standard but rather in the sense that no standard of conduct is specified at all." *Id.* at 614.

The vice of vagueness, particularly one touching first amendment freedoms, was set forth in *Graynard* v. *City of Rockford*, 408 U.S. 104, 108, 92 S. Ct. 2294, 2299 (1972):

> "It is a basic principle of due process that an enactment is void for vagueness if its probihitions are not clearly defined. Vague laws offend several important values. First, because we assume that man is free to steer between lawful and unlawful con-

duct, we insist that laws give the person of ordinary intelligence a reasonable opportunity to know what is prohibited, so that he may act accordingly. Vague laws may trap the innocent by not providing fair warning. Second, if arbitrary and discriminatory enforcement is to be prevented, laws must provide explicit standards for those who apply them. A vague law impermissibly delegates basic policy matters to policemen, judges, and juries for resolution on an ad hoc and subjective basis, with the attendant dangers of arbitrary and discriminatory application. Third, but related, where a vague statute 'abut[s] upon sensitive areas of basic First Amendment freedoms,' it "operates to inhibit the exercise of [those] freedoms.' Uncertain meanings inevitably lead citizens to ' "steer far wider of the unlawful zone" * * * than if the boundaries of the forbidden areas were clearly marked.' (Footnotes omitted.)

Where first amendment freedoms are involved a greater degree of specificity is required than in other context. *Smith* v. *Goguen,* 415 U.S. 566, 573, 94 S. Ct. 1242, 1247 (1974). The bill's standard fails to meet this exacting test, when applied to solicitations made by religious and charitable organizations.

Second, the objectional quality of vagueness and overbreadth in the bill is aggravated by the section of the bill permitting a private citizen to sue if he or she feels harrassed, oppressed or abused by a solicitation. The concern here is the potential for arbitrary and harrassing lawsuits by disgruntled recipients of unwanted telephone calls.

In *Riley* the Court pointed to the potential costs of litigation stating that "[t]his chill and uncertainty" might drive professional fundraisers out of an area, "or at least encourage them to cease engaging in certain types of fundraising (such as solicitations combined with the advocacy and dissemination of information) or representing certain charities (primarily small or unpopular ones), all of which will undoubtedly 'reduc[e] the quantity of expression.' " 108 S. Ct. at 2676.

Because religious and charitable solicitations are fully protected by the first amendment, regulation of a solicitation "must be undertaken with due regard for the reality that solicitation is characteristically intertwined with information and perhaps persuasive speech * * *, and for the reality that without solicitation the flow of such information and advocacy would likely cease." Riley at 2677 quoting *Schaumburg.* For the foregoing reasons the bill should be amended to exempt religious and charitable solicitations.

STATEMENT OF THE AMERICAN RESORT AND RESIDENTIAL DEVELOPMENT ASSOCIATION

I. ARRDA AND GROWING SELF-REGULATION BY ITS MEMBERS

Mr. Chairman and Members of the Subcommittee, on behalf of its nearly 800 members throughout the United States, ARRDA appreciates the opportunity to provide its views on telemarketing and other fraud legislation, S. 2213, S. 2326, and H.R. 4101.

ARRDA's membership consists of developers, operators, and owners of resort and residential communities located throughout the United States. Firms that belong to ARRDA also include vacation exchange companies, lenders, consultants, attorneys, and accountants who provide services needed by members and consumers. Our members include large and small businesses, both corporate and individually owned.

Each year, ARRDA's members serve millions of consumers in the United States and abroad by providing the varied leisure opportunities that families and individuals want and need in today's society. Since its founding in 1969, ARRDA has worked hard to improve the quality of Americans' vacation and recreational experiences.

ARRDA shares your concerns about fraud from telemarketing and other sources. Our customers, our members, and our members' suppliers suffer financially when fraud or other improper conduct occurs.

This is one reason why a critical part of ARRDA's effort has been to take an active role in government regulation and our industry's self-regulation. For nearly 20 years, we have worked with federal and state legislators, regulators, and enforcement officials to draft needed laws and rules and provide guidance on other necessary actions.

Examples of such cooperation are numerous and continuous. They include the following:

Significant input on extensive amendments to the Interstate Land Sales Full Disclosure Act and Regulations in the 1970s and 1980s

Joint efforts with state legislators and regulators on vacation timeshare legislation in over 30 states

The creation of model vacation timeshare laws

Aiding government officials in writing their consumer education materials

Within our industry, ARRDA has played a growing role in self-regulation to make our members more sensitive and responsive to our customers. Consumer education booklets make buyers more knowledgeable. Our frequent seminars featuring elected representatives, government officials, and industry leaders have raised the legal compliance and professionalism of our members.

Further evidence of our commitment to high quality projects and consumer satisfaction is our recently strengthened Code of Standards & Ethics. As the Preamble states:

"[ARRDA] and its members are committed to the highest standards and ethics in resort, recreational, residential, and community developments for the benefit of the public. * * * All activities subject to this Code shall be designated to be honest and fair, and to be conducted with integrity, dignity, and propriety."

Our Code binds members and nonmembers using members' services. It applies to developers and all service firms, whether they engage in any aspect of project development or in marketing, such as telemarketing.

Each member involved in these activities must comply with all federal, state, and local laws and regulations. Statement conveyed in any manner, including by telephone, may not false or deceptive information or omit material information.

The Code contains fair, but comprehensive, enforcement provisions. Apparent violations are investigated. Where improper conduct is not corrected, ARRDA may impose appropriate sanctions, including expulsion from membership. Publication of the results of an inquiry may result in action by government officials.

To reinforce the goals of the Code and enhance professional performance of members' employees, ARRDA has recently begun the ARRDA Education Institute. For a member to join the Institute, it must comply with the Code and applicable laws and regulations. Its personnel must complete an educational course and pass an exam.

II. COMMENTS ON PRESENT LEGISLATION

ARRDA favors passage of amendments to the Federal Trade Commission Act that would effectively curb telemarketing and other fraud. Unfortunately, despite their worthy objectives, each of the present bills has sufficient flaws that deter us from supporting them in their current form.

Moreover, the vast number of variables that arise in business use of telephones makes it desirable, in ourview, to postpone further consideration until adequate input can be provided by all affected parties. We have commented below on some of our major concerns.

A. "Telemarketing" Is Defined Too Broadly

Those, including ARRDA, who favor appropriate legislative curbs and remedies for telemarketing fraud, seek effective ways to deal with abuses in the marketplace. Yet, the definition of "telemarketing" in this legislation fails to focus only on the perceived problem area. All three bills define "telemarketing" to include "every use of a telephone in the ordinary course of business to communicate * * * an offer for sale or to complete a sale of a product or service."

This definition extends well beyond the types of telemarketing covered in the Senate and House hearings on these bills. It may be construed to cover virtually each use of a telephone that is in any way, however tangential, connected to the marketing or delivery of virtually any product or service.

Dealings between a legitimate seller and business or consumer buyer could be affected simply because of one telephone call. For example, a single call, or possibly a telecopier (FAX) message, from a buyer to tell the seller to *delay* a delivery date could bring the entire transaction within the scope of these bills.

Given the extremely broad scope of the Federal Trade Commission Act, this type of definition could intrude on the vast majority of businesses operating in this country. Retailers, hotels, doctors and other health care providers, firms providing personal and business services of all types, real estate companies, and countless others could face this new layer of regulation. Instead of applying only to the more than $100 billion in estimated telemarketing revenue, these bills would cover trillions of dollars in annual sales throughout the American economy.

This definition would unfortunately and unnecessarily apply where telephone usage is incidental and the actual sale occurs in person. This is true in many industries, including ours. Consumers who are interested in learning about a vacation retreat or other property usually initiate the call that results in an appointment to inspect the property. They typically spend many hours, or even days, at the site and receive extensive disclosures before deciding whether to buy.

Requests for vacation exchanges and similar services are also initiated by consumers after they have made on-site purchases and joined exchange clubs. These services permit owners in one property to trade for the use of lodging in another project. After buying a resort interest, consumers receive large directories listing hundreds of available resorts. They review this information before calling or mailing in their selections.

Nearly all exchange requests are filled, and consumers do not pay for an exchange unless a request is filled in a way that satisfies them. The major vacation exchange companies use toll-free phone lines to receive calls from existing members around the world.

These firms do not make random calls to nonmembers to ask them to join the exchange service or to make trades. As noted above, membership begins only after a consumer actually visits a resort and decides to purchase a vacation timeshare. In processing requests for trades, the exchange companies deal with pre-existing members, who have belonged for as long as ten years or more, and who initiate the request for a trade. In so doing, the members are simply exercising their rights under enforceable contracts with the exchange firms. Telephones simply expedite the effective processing of requests *from* consumers who already belong.

Likewise, telephones assist in the renewal of exchange memberships by existing members. On the basis of their past experience with an exchange company, existing members may decide to renew or not to do so. The leading exchange companies, which have been operating successfully for many years, obviously cannot initiate random calls to *nonmember* consumers to invite them to *renew* an exchange membership that, by definition as nonmembers, they do not have.

Our industry and many others are already heavily regulated at the federal, state and local levels. Substantive legal protections and disclosure requirements are comprehensive. Consumers and businesses have significant rights pursuant to common law and statutes, including consumer protection laws, in every state.

The broad definition of "telemarketing" in the three bills under consideration could complicate and interfere with legal compliance by legitimate firms arising from their use of telephones. By imposing regulation where it is not needed, these bills could raise costs to buyers and make it more difficult for sellers to satisfy their needs.

B. Automatic Cooling Off Periods May Be Disruptive and Costly for Many Customers and Businesses

Mandatory cooling off periods may arise under these bills in connection with covered telemarketing activities. Just as no such requirement applies to all mail order sales under the Federal Trade Commission's Mail Order Rule, which is the model for these bills, none should apply automatically to "telemarketing" as it is now defined.

Imposing a cooling off requirement would be undesirable in many instances. Prompt shipment of ordered merchandise, within the stated delivery time, complies with the Mail Order Rule.

Such responsiveness to buyers should have a similar effect in telemarketing. This is especially true where there is an existing buyer-seller relationship and the buyer is purchasing from a catalog or other document that could be used for a mail order. The choice of whether to mail or call in an order to a reputable firm should not change a buyer's rights. Customer satisfaction should not be hindered or delayed by imposing an automatic cooling off period.

Similarly, time-sensitive delivery of products and services could be harmed by requiring a cancellation period. Perishable foods, flowers, and other goods, travel and lodging services, and, within our industry, vacation exchange services are within this category.

To provide the vacation exchange opportunities described above, our members have spent vast sums on complex computer hardware and software. The exchange process is complicated, because each consumer chooses several possible trades in a specified time period from among many hundreds of resorts.

Computers have to match resorts chosen with those available for thousands of consumers seeking trades at any given time, and counsellors need to communicate options promptly with members for the process to function properly. At this point it works so well that hundreds of thousands of trades occurred last year.

In recent years, the exchange companies have expanded their capabilities to offer exchanges within as little as one or two days of the date when the facilities will be available. The very nature of these offerings makes time even more critical than in normal exchanges, where consumers have more time to decide. Rapid, if not immediate, consumer decisions must be made if an option is to be used. During high demand times, such as Christmas and New Year's, this is especially true.

Consumers who are interested in these last-minute trades use their directories for needed facts about the resorts where space is being offered. Exchange counsellors answer additional questions in order to help them make wise decisions. Many satisfied consumers have benefitted from these short-term offerings.

Unfortunately, requiring a cooling off period for all trades could sharply curtail this service and make it more expensive. Consumers would then be deprived of enjoyable vacations and pay more for those they are able to take.

C. A Strengthened FTC Should Direct Uniform Enforcement Efforts

Most parties testifying or providing statements concerning these bills agree on the desirability of effective laws to prevent and remedy telemarketing fraud. They disagree on the specific powers to be granted, and to whom they should be provided.

In the interest of uniform national enforcement policy, we believe that the Federal Trade Commission should play the central role under the Federal Trade Commission Act. It acts only when it has carefully determined that it is in the "public interest" to do so, and it has more experience under that statute than any state consumer protection office. The FTC's ability to act quickly and effectively would rise with expanded enforcement tools of the types proposed in S. 2326.

1. Role of Attorneys General

Appropriate assistance from state attorneys general to the Commission, on a case-by-case basis, may be a desirable way to increase responsiveness and reduce time before necessary corrective action is taken. Commission control is vital, however, in our opinion to avoid state actions that are duplicative of or inconsistent with other federal or state actions.

In addition, the Commission may be more responsive to the needs of all Americans, rather than those in one or a few states, who are affected by telemarketing or other fraud. The Commission has 10 regional offices located throughout the United States, and its activities are financed by contributions from every taxpayer, not just those in a single state.

Its national scope also gives the Commission the greatest ability to enforce uniformly any orders that may arise from cases. Such uniformity is vital to the effectiveness of the numerous FTC orders already in place, as well as those issued in the future under the FTC Act. Without Commission direction of litigation efforts, a patchwork of misguided cases and inconsistent orders could readily emerge.

2. No New Private Rights Needed

We are opposed to the creation of private rights of action in federal court under S. 2213 and H.R. 4101. Consumers, businesses, and other parties injured in part as a result of fraudulent conduct involving use of a telephone already have substantial rights under state statutes and common law.

For example, fraud, a necessary ingredient for a claim under both bills, is one of the most well-established bases for recovery in all 50 states and the District of Columbia. Each state and the District of Columbia also has a "Little-FTC Act," most of which permit private actions on a more liberal basis than where fraud must be proven. Where a federal claim is justified, the Civil RICO Act (18 U.S.C. § 1964(c)), provides more than ample remedies, as Judge Schwartzer's statement on behalf of the Administrative Office of the U.S. Courts indicates.

A single call should not transform a potential state court contract claim into a federal matter. Otherwise, the result could be a vast rise in federal cases filed, with delays in more substantial and meritorious cases. We concur in the concerns expressed by Judge Schwartzer about the extremely harmful effect of such provisions on the caseload in the federal courts. The $10,000 threshold in the House Bill does not eliminate this concern, as punitive damages and other claims unrelated to actual out-of-pocket losses could readily pass this barrier.

III. INPUT ON FUTURE LEGISLATION

We have discussed above some of our major reservations about the pending bills. Given the short time remaining in the current session, we believe that enactment of any of the pending bills would be inadvisable.

It would be preferable to address these issues again in 1989. If legislation is desired, we would welcome the opportunity to work with concerned legislators and their staffs to draft appropriate provisions. Taking this additional time should result in a bill that helps consumers *and* legitimate businesses that use the telephone as an essential tool in serving those consumers.

STATEMENT OF THE AMERICAN ARTS ALLIANCE

The American Arts Alliance, a consortium of nonprofit, performing, exhibiting and presenting arts institutions, appreciates the opportunity to submit this statement to the Senate Commerce Subcommittee on Consumer. We commend the Subcommittee for its interest in addressing the issue of telemarketing fraud, and certainly recognize the need to combat abuses in this area. We do hope, however, that during deliberations the Subcommittee will take special care to target offenders without punishing legitimate organizations.

Arts institutions have come to depend heavily on telemarketing as a means of reaching arts patrons and providing valuable program information to the public. As the effectiveness of direct mail declines, an increasingly large number of arts organizations are turning to telemarketing. An informal survey of our members representing the dance, opera, symphony and theater disciplines showed that, on the average, 60% of total ticket sales are conducted by telephone.

Telemarketing is a key component in the financial equations of arts organizations all over the country. Faced with reductions in government grants and increased competition for private contributions, performing arts institutions are more and more reliant upon earned income. Telemarketing has proven extremely effective as a means of boosting ticket sales and increasing community awareness of upcoming cultural events.

In the course of our survey we learned that nonprofit performing arts institutions engaged in telemarketing conduct sales campaigns three to six months preceding their performance seasons. Season tickets sold during these months provide a significant portion of an organization's financial base.

During a telemarketing campaign, outbound telemarketing calls are generally made between 5:15 and 9:30 p.m. on weekdays, though a few of the institutions surveyed begin calls at 9:00 a.m. The American Arts Alliance believes this practice is reasonable and analogous to the approach taken by legitimate telemarketing entities nationwide.

The vast majority of arts patrons react positively when hearing from representatives of arts organizations. These calls provide a human element and are presented as a service communicating important information concerning seating, performance dates and ticket prices is readily available. Telemarketing is convenient and benefits prospective customers in a manner other marketing practices cannot. It is an effective direct response medium which allows the public the convenience of ordering tickets over the phone either by personal check or credit card.

According to our survey, ninety percent of all telephone ticket sales are charged to credit cards. Normally, the customer's account reflects the purchase immediately and written confirmation of the sale in often provided for the patron's records.

Tickets are delivered to patrons in advance of the performance season. However, if an order is taken early during the telemarketing campaign, several months may pass before the ticket is actually in the hands of the patron. This would seem unreasonably long by ordinary product marketing standards, but in the context of the arts world, it is quite feasible for the bulk of an organization's season tickets to be mailed at the same time, two to four weeks prior to a performance season. This system is functioning efficiently for arts institutions all over the country, and no organization contacted through the course of our survey cited delivery time as a source of patron complaint.

Most of the arts institutions participating in our survey reported very few grievances. Less than two percent of their total ticket sales end in refund, though many organizations offer full refunds for any reason up to twenty-four hours prior to a performance. The most common basis for refund requests were relocation, death, and illness, and rarely involved patron dissatisfaction.

Maintaining a positive public image and community rapport have always been priorities throughout the arts community. Accordingly, particular attention is given to courtesy, convenience and willingness to accommodate patron preferences. Arts organizations are exceedingly cautious of how they are perceived and represented to the publics they serve, and this caution certainly encompasses their marketing endeavors.

In summary, it is clear that nonprofit arts institutions are to be counted among the legitimate telemarketers in this country. Like consumers, arts groups are falling victim to the negative climate created by telemarketing fraud. Should Congress deem it necessary to address the problem of telemarketing fraud through legislative or regulatory measures, it is vital that offenders be targeted without placing undue restrictions on legitimate telemarketers, such as the arts groups we so proudly represent.

STATEMENT OF THE NATIONAL FEDERATION OF INDEPENDENT BUSINESS

Mr. Chairman, on behalf of its over 500,000 members nationwide, NFIB is pleased to submit this statement concerning H.R. 4101 and S. 2213, The Telemarketing Fraud Prevention Act of 1988.

Literally thousands of our members use telemarketing operations in the course of their daily business. NFIB therefore welcomes genuine and effective efforts to address telemarketing fraud. The damage and distrust which can result from fraudulent telemarketing is harmful to *all* legitimate business operations.

We do have some practical difficulties, however, with aspects of the legislation as passed by the House on June 28, 1988. While the bill's goals are worthy, its scope and vagueness threaten to drag many legitimate businesses into court, while allowing the fraudulent operators to escape justice. Additionally, we submit that this issue has not been accorded the review process it deserves. *It is an extremely important matter for the majority of businesses, large and small, in this country*, and may put many of them in a precarious position with regard to their day-to-day business operations. We should therefore exercise caution and pursue a reasonable, effective approach. Overreaction will not solve this nationwide dilemma.

DEFINITION OF "TELEMARKETING" TOO BROAD

NFIB feels that the definition contained in H.R. 4101 goes too far beyond the scope of what would normally be considered "telemarketing".

Specifically, H.R. 4101 states that any "use of a telephone in the ordinary course of business to communicate an offer for sale or to complete a sale * * *" can be considered "telemarketing" (with the exception for the "occasional use of a telephone by a person to sell, for example, his or her house or car * * *").

This could conceivably include *virtually any commercial use of the telephone* in any standard business operation. Businesses like real estate, mail order sales, wholesale sales, insurance and financial products, and service industries would be severely affected. Countless *small firms* rely on the telephone in the absence of sophisticated computer marketing systems. With this broad definition as a standard, *all related marketing and advertising practices* could be subject to sweeping restrictions under the bill.

Additionally, the language of H.R. 4101, specifically Section 2(e), remains unclear as to whether telemarketing "service bureaus" are included under the bill's coverage. These middlemen in the marketing operation, while *not actually involved in sales of products*, are involved in the payment system and eventual completion of the sale. They are, in effect, independent contractors who assist in the taking of orders, pass those orders on to the business, and then are *out of the loop*. They take incoming calls only, and are not directly involved in the product's advertising or sales. As such, we respectifully respect clarification of this section to eliminate telemarketing service bureaus from coverage.

ENFORCEMENT AUTHORIZATION

The sweeping enforcement authority granted in H.R. 4101 is excessive and unprecedented. Under this bill, state attorneys general, other state officials, *and* private parties—including competitiors—are authorized to seek redress in federal courts against telemarketers whom they deem "fraudulent" (not defined in the bill) or who violate a not-yet-determined FTC rule.

In practical terms, this authority is simply too broad. It literally grants state officials authority to dictate the advertising and marketing activities *of any business* using a telephone as a sales tool.

In allowing the state attorneys general to bring suit against a telemarketer in another state because they allege that the telemarketing practice "affects" their state or its residents, we invite chaos and inconsistency. Overburdened courts and inconsistent court interpretation *and* enforcement are sure to result. These businesses would be subject to lawsuits brought by federal authorities nationwide, state AGs from their states, state AGs from any other states, *and* private parties.

For retailers, especially those operating multi-state catalogue sales companies, the prospect of having to keep track of legal activities and telemarketing laws in all 50 states is daunting, not to mention unreasonable. Many catalogue sales companies are small businesses that simply don't have the resources to contend with this maze of requirements. Requiring them to do so *guarantees* a cutback on jobs and/or consumer services, since it adds to their cost of doing business.

We would submit that there is no demonstrated need for additional grants of enforcement authority beyond those provided under current law.

RECOVERY OF LEGAL COSTS

Also of concern to NFIB is the potential financial injury to a *ligitimate* telemarketer involved in a suit. While an individual who successfully brings suit against a telemarketer is allowed to recover legal fees, a legitimate telemarketer who ultimately prevails against the plaintiff is prohibited from recouping the costs of their defense. This is an unfair and one-sided approach, and should be corrected.

CLEARINGHOUSE

The clearinghouse recently established by the FTC and the state AGs to collect data to track down fraudulent telemarketers is a step in the right direction. This automated databank, though currently being accessed by only about twenty-two states, should be encouraged and evaluated before we go into sweeping legislation to impose restrictions on business practices.

CONCLUSION

NFIB welcomes the Congress' efforts to eliminate the fraudulent telemarketers from the market. We urge the Committee to review carefully the problems we see arising from H.R. 4101/S. 2213 in their current forms, and make the appropriate changes which will ensure that fraudulent telemarketers are dealt with and legitimate telemarketers remain free of needless regulation. With appropriate measures taken to ensure that legitimate businesses aren't put out of business by this legislation, we can achieve an improved business climate that will benefit both consumers *and* businesses.

Statement of the Air Transport Association of America

The Air Transport Association of America ("ATA") represents most of the scheduled airlines in the United States. Collectively, ATA member airlines operate over 97 percent of the revenue passenger miles, and about the same percentage of freight miles, flown domestically by U.S. carriers. We are pleased to submit to this Subcommittee our statement concerning the pending telemarketing fraud prevention bills, and the impact which these bills, if passed, would have on the airline industry.

At the outset, let us state that this legislation does not pit "business" against "consumers," and the issues should not be perceived in that context. The airline industry, although the nature of its injury may be different, has suffered as much as individual consumers as a result of fraudulent schemes perpetrated by these con artists. Every time a travel or vacation scam occurs, the integrity of the airline industry suffers. For this reason, we hope that we can work with this Subcommittee in formulating legislation which does not adversely impact the accepted and legitimate telephone sales and service practices of the airline industry, practices which the public expects and upon which it relies.

The purpose of each of these bills (S. 2213, S. 2326, and H.R. 4101) is to address the growing problem of fraudulent sales schemes conducted by telephone, loosely described as "telemarketing fraud." To attack this problem, these bills would expand FTC authority to regulate telemarketing activities, authorize state attorneys general to enforce such Federal Trade Commission ("FTC") regulations (and state laws and regulations) in Federal court, and allow private citizens to bring civil actions in federal court on the same basis.

The problem with the proposed legislation stems from the definition of the term "telemarketing." Each of these bills defines telemarketing as follows: " 'telemarketing' is the use of a telephone in the ordinary course of business to communicate with a person an offer for sale or to complete a sale of a product or service."

This definition is so broad that *it captures airline and travel agent reservations activities.* Even though many sales may not be completed by a telephone communication between a consumer and a reservations or ticket agent, such communications clearly fall within the definition of telemarketing as "an offer for sale * * * of a product or service."

The legislation is well intentioned and, judging from horror stories reported in the media, much needed. However, because the Department of Transportation ("DOT") closely regulates the consumer aspects of airline activities, the reservations and ticket sales activities of airlines and ticket agents should be excluded from the scope of this legislation. Not only is legislation not needed, but it would create confusion and uncertainty by giving both the DOT and the FTC authority over the same activities.

A. *Existing Consumer Protection.*—Consumers are adequately protected by provisions of the Federal Aviation Act, as amended, and existing DOT regulations. Pursuant to § 401(d)(1) of the Federal Aviation Act, DOT has broad authority over all certificated air carriers. Section 401 requires certificated air carriers to be fit, willing, and able to perform transportation services "properly and to conform to the provisions of this Act and the rules, regulations, and requirements of the [Department]." 49 U.S.C. App. § 1371(d)(1).

More specifically, and more to the point, § 411(a) of the Federal Aviation Act (49 U.S.C. App. § 1381(a)) authorized the Department to investigate and determine whether any air carrier or ticket agent has engaged in "unfair or deceptive practices." The Department has interpreted § 411 broadly, promulgating rules, regulations and policy statements prohibiting a broad range of deceptive practices and establishing a formal enforcement mechanism. For example, under 14 C.F.R. § 202.2, an intentional failure by a certificated carrier to comply with the Act, a DOT order, rule or regulation, or any term, condition, or limitation of its certificate, is deemed a certificate violation subjecting the carrier to enforcement action.

Regulations addressing specific airline conduct include: the filing of service quality performance reports with respect to on-time performance and baggage handling (14 C.F.R. Part 234); notice of terms of contract of carriage required to be printed on tickets, including notice of certain terms concerning refunds, ticket price and penalties (14 C.F.R. Part 253); domestic baggage liability (14 C.F.R. Part 254); strict rules concerning airline oversales and denied boarding (14 C.F.R. Part 250); prohibiting carrier activities which tend to pass off the service of one carrier as the services of another (14 C.F.R. § 399.82); and strict control of charter operations and activities (14 C.F.R. Parts 207 and 208). Additional related provisions require carriers to preserve records of consumer complaints and evidence of compliance with regulations implementing certain provisions of the Consumer Credit Protection Act.

DOT similarly regulates the practices of ticket agents. 14 C.F.R. § 399.80 prohibits a broad array of misleading or deceptive practices by ticket agents, and subjects ticket agents to enforcement action in the event of a violation of those regulations.

With respect to price advertising, DOT has issued a formal policy statement found at 14 C.F.R. Part 399.84. In fact, DOT has taken the position that it has preempted the field to the exclusion of state regulation of airline advertising practices.

DOT regulations also establish procedures for enforcement proceedings, whether commenced by the Department or upon the complaint of a third party. The Department has authority to grant various forms of relief, including assessment of penalties, cease and desist orders and certificate action.

The conclusion to be drawn is that it is not necessary for the proposed legislation to reach airline and ticket agent "telemarketing" hose practices. Adequate protection for consumers exists in current regulations, and the Department is active in enforcing those regulations. For this reason alone, certificated air carriers and ticket agents should be exempted from the scope of the proposed legislation.

B. *Dual Jurisdiction Will Create Confusion.*—An additional reason for exempting certificated air carriers and travel agents is that giving the FTC regulatory authority over their telemarketing practices results in two agencies, DOT and FTC, having regulatory authority over the same area. This can only lead to confusion, uncertainty and conflicting requirements. It will also unnecessarily cause the waste of federal resources.

The same reasoning applies to the proposal to grant state attorneys general and private citizens enforcement authority with respect to airline telephone reservations and sales practices. Confusion, uncertainty and inconsistent requirements will occur, and unnecessary litigation against legitimate businesses will abound. Authorizing litigation, whether by a state attorney general or a private citizen, is inconsistent with the detailed and effective administrative regulatory mechanism now in place.

STATEMENT OF BELL ATLANTIC CORP.

Bell Atlantic Corporation submits this Statement on behalf of its operating telephone companies serving telephone subscribers in new Jersey, Pennsylvania, Delaware, Maryland, Virginia, West Virginia, and the District of Columbia.

The Telemarketing Fraud Prevention Act of 1988, S. 2213, addresses a national problem involving misuse of telephone services. Because Bell Atlantic shares the Subcommittee's concern that our telephone services may be subject to misuse by a small portion of our subscribers, we have carefully reviewed the bill's provisions.

S. 2213 defines the term "telemarketing" to mean "the use of a telephone in the ordinary course of business to communicate with a person or offer for sale or to complete a sale of a product or service." By that definition virtually hundreds of thousands of routine calls which take place daily between Bell Atlantic's employees and our customers concerning the services we offer become subject to the terms of this bill.

Bell Atlantic believes this definition is unnecessarily broad and urges this Subcommittee to modify the definition of "telemarketing" as follows:

"(k) For purposes of this section, the term 'telemarketing' means the use of a telephone in the ordinary course of business to communicate with a person an offer for sale or to complete a sale of a product or service; *provided, that 'telemarketing' shall not include activities relating to the sale of telecommunication services or products subject to regulation by the Federal Communications Commission or by state or local public utility regulatory bodies.*"(New text underlined)

Congress has already directed that the Federal Trade Commission is not empowered to regulate "common carriers subject to the Acts to regulate commerce" [15 U.S.C.A. § 45(a)(6)]. Therefore, Bell Atlantic's proposed text constitutes a technical and conforming amendment and is fully consistent with existing law, eliminating any doubt that Bell Atlantic's operating companies will not be subjected to duplicative and inconsistent directions.

The amendment Bell Atlantic is proposing does not in any manner undermine the effectiveness of the bill. In our opinion, because the proposed amendment only excludes those activities that are subject to regulation, the effectiveness of the bill is improved by avoiding the problem of duplicative and potentially inconsistent standards and decisions by the Federal Trade Commission, on the one hand, and the Federal Communications Commission and state and local regulatory agencies on the other.

The Federal Communications Commission and the state regulatory agencies already provide adequate forums for redressing customer complaints. If Bell Atlantic's proposed amendment is adopted, these agencies may continue to use their long-established expertise and knowledge of the telecommunications common carrier business to address matters subject to their jurisdiction without having to consider how their decisions affect the Federal Trade Commission's decisions under this bill. At the same time, the Federal Trade Commission can direct its resources to other areas where, as this bill recognizes, our subscribers lack effective recourse.

For these reasons, Bell Atlantic urges this Subcommittee to revise the bill as proposed.

U.S. Chamber of Commerce

1615 H Street, N.W.
Washington, D.C. 20062
202/463-5602

Albert D. Bourland
Vice President
Congressional Relations

September 15, 1988

The Honorable Albert Gore, Jr.
Chairman
Subcommittee on Consumer
Committee on Commerce, Science and
  Transportation
U.S. Senate
Washington, D.C. 20510

Dear Mr. Chairman:

The U.S. Chamber of Commerce, the world's largest federation of businesses, chambers of commerce and trade and professional associations, offers its views on your bill S. 2213, the Telemarketing Fraud Prevention Act of 1988, the House-passed version H.R. 4101, introduced by Representative Luken (D-OH), and S. 2326, the Consumer Fraud Prevention Act, introduced by Senator McCain (R-AZ).

The Chamber shares the Subcommittee's concern regarding the problems associated with fraudulent telemarketing activity. Such activity not only defrauds a broad cross section of American consumers but also undermines legitimate business opportunity.

While the Chamber strongly supports appropriate efforts to eradicate telemarketing fraud, it believes that S. 2213 and H.R. 4101 are in certain sections duplicative of existing law and would encourage additional litigation in the already burdened federal court system.

Under existing law, most states are capable of acting effectively against fraudulent telemarketing activity. Consumer protection statutes, which generally include language that makes unfair or deceptive acts or practices affecting commerce actionable, empower the states to take decisive civil action against telemarketing fraud. In addition, state criminal laws against fraud generally permit criminal prosecution of fraudulent telemarketers.

S. 2213 and H.R. 4101 would also authorize suits under Section 19 of the Federal Trade Commission (FTC) Act by private parties against those who engage in fraudulent telemarketing activity. Most states have passed laws that enable private parties to seek monetary redress against those who perpetrate fraudulent schemes, under fraud or breach of contract theories. Furthermore, in light of the private right of action available under the Racketeer

Influenced and Corrupt Organizations Act, the Chamber is opposed to any further federalization of the common law fraud action.

The Chamber is also concerned that S. 2213 and H.R. 4101 would create a new class of federal litigants. Under both, defendants are broadly defined as "all sellers of goods by telephone," and plaintiffs are empowered with an overly broad statutory right of action in fraud, which the Chamber believes would encourage unnecessary federal court litigation. The Chamber also believes that the provisions of S. 2213 and H.R. 4101 that would allow state officials, state attorneys general and private parties access to federal court in these matters would further burden the federal court docket.

S. 2326 is an alternative approach to this pervasive problem that the Chamber supports and encourages the Subcommittee to consider. It would authorize the FTC to appoint state attorneys general to assist FTC attorneys as the need arises. The Chamber believes that this bill would accomplish many of the Subcommittee's desired goals without having an adverse effect on the federal court case load or duplicating present state consumer protection efforts.

The Chamber requests that S. 2213 and H.R. 4101 be comprehensively reviewed prior to further consideration by the Subcommittee and that this letter be made part of the hearing record.

Sincerely,

Albert D. Bourland

UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

OFFICE OF
THE COMMISSIONER

September 17, 1988

The Honorable Albert Gore, Jr.
Chairman, Consumer Subcommittee of the
  Committee on Commerce, Science and
  Transportation
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for this opportunity to present my views supplementing the testimony of the Federal Trade Commission ("Commission" or "FTC") on various legislative initiatives aimed at combatting telemarketing fraud. I also have taken the liberty of enclosing a recent speech before the National Association of Consumer Agency Administrators addressing this topic at greater length. The Subcommittee's keen interest in attacking this enormous problem is heartening and promises to be of major benefit to consumers across the country.

The status quo simply is unacceptable. It is intolerable that American consumers are being bilked by telemarketing con artists to the tune of some $1 billion a year. These fraudulent operators literally have defrauded well over a million citizens of their hard-earned dollars. As a result, these few "bad apples" -- and the fear they have created -- threaten the business of legitimate telemarketing operations. The vast majority of honest telemarketers can not survive without the trust of their customers. That trust becomes increasingly fragile as tales of deceitful activities within the industry proliferate. At stake, then, is not only the well-being of consumers, but also the economic health of an industry with sales of approximately $120 billion annually.

As far as the FTC's role in fighting telemarketing scams is concerned, two reactions are appropriate: pride and frustration. Pride is justified by the dedicated effort staff has made to stem this tide of fraud. The Commission's testimony offers numerous details about the many notable accomplishments of staff in recent years, often achieved against long odds and under great time pressure.

Sad to say, there also is reason for frustration. For our efforts have been overwhelmed by an avalanche of fraudulent operations. To put this in perspective, consider a few summary statistics.

Since December 1982, the FTC has brought 29 federal district court cases against nationwide telemarketing frauds. So far, through these actions, the Commission obtained judgments for over $80 million and actually secured roughly $23 million of that amount for redress to scam victims. Checks have been sent to more than 6,500 victims.

Unfortunately, these figures are a drop in the bucket given that the aggregate sales in these 29 cases alone were over $624 million, and that an estimated 1.1 million consumers were victimized in the process. Of course, this does not even begin to reckon with the unknown number and amount of telemarketing frauds for which no FTC case has been filed to date.

This is the background that appropriately has created a sense of urgency in legislative deliberations on the bills introduced to change this situation. In this context, it is all the more vital that state and federal officials redouble their efforts to fashion a unified approach to maximize their effectiveness, rather than going their separate ways. For that matter, while I share the Commission's concern that the delegation of authority to state and local officials proposed in some of these bills holds the potential for "inconsistent law and adverse decisions," that concern is muted by the overall gravity of the circumstances and the legal and budgetary limitations constraining FTC enforcement work.[1]

Accordingly, I would like to emphasize my support for the legal "relief provisions" contained in Senate Bill 2326 as described in the Commission testimony. Regarding the budget aspect, it is axiomatic that with extra resources the FTC could bring more meritorious cases against telemarketing fraud and engage in a greater variety of cost-effective consumer eduction projects. The trend, however, has been in the other direction. While the FTC had 530 workyears devoted to its consumer protection mission in fiscal year ("FY") 1981, and 444 workyears in FY 1984, it has only 349 workyears in FY 1988 and unless something changes, that figure is likely to drop dramatically in FY 1989.

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[1] I continue to think that if legislation conferring new rights of action to individuals or states is to be enacted, it would best be done as a separate statute. This would avoid any potential for "inconsistent law and adverse decisions" affecting agency operations under the FTC Act.

For all the above reasons, it is crucial that any new law appreciably strengthens the various enforcement agencies in their struggle against telemarketing fraud without creating unintended and counterproductive consequences. If we fall short of that mark, who knows how many more years will pass -- and how many more consumers will be hurt severely -- before a chance to enact corrective legislation will arise?

I conclude, then, with a plea to all who have contributed to the progress of these bills to unite in the interest of an end result that will best serve the public. Of course, I am at the Subcommittee's disposal if I may be of any assistance in this endeavor at any time.

Sincerely yours,

Andy Strenio

Andrew J. Strenio, Jr.
Commissioner

Enclosure

U.S. Department of Justice

Office of Legal Policy

Assistant Attorney General

Washington, D.C. 20530

27 SEP 1988

Honorable John McCain
United States Senate
111 Russell Senate Office Building
Washington, D.C. 20510

Dear Senator McCain:

This is in response to your request for the views of the Department of Justice concerning S. 2213, S. 2326, and H.R. 4101, three bills that address fraudulent telemarketing activities. For the reasons set forth below, the Department does not support the approach taken in S. 2213 and H.R. 4101, but has no objection to passage of S. 2326.

Each bill is designed to strengthen enforcement efforts against consumer fraud committed by means of telemarketing, a goal that the Department wholeheartedly endorses. Both S. 2213 and H.R. 4101 provide for expanded enforcement by amending the Federal Trade Commission Act to allow state attorneys general (or other state officers with authority to enforce consumer protection laws) and private citizens to bring civil actions in the federal courts against those who engage in telemarketing that is fraudulent or in violation of an FTC rule. S. 2326 adopts a different approach by expanding the authority of the Federal Trade Commission. It recognizes, in proposed section 4(e), the value of cooperation with state attorneys general by authorizing the Commission to appoint them to assist its efforts in enforcing FTC rules when the public interest so requires.

We do not believe that the approach taken by S. 2213 and H.R. 4101 is advisable. Suits by state authorities and private citizens have the potential of interfering with enforcement efforts by the Federal Trade Commission and the Department of Justice, of leading to inconsistent application of the law, and of burdening the federal courts with litigation that more properly belongs in the state courts. In the latter regard, we note that state authorities and consumers already have available a wide range of preventive and remedial measures for dealing with telemarketing fraud. These include state criminal laws against fraud, the federal "RICO" statute, 18 U.S.C. § 1962(c), state "little RICO" and "little FTC" statutes, and common-law actions for fraud or breach of contract. Moreover, creation of federal causes of action dealing specifically with telemarketing fraud could lead to pressure to provide federal remedies for other forms of fraud as well, a development that we do not think would be in the public interest.

We also oppose the passage of H.R. 4101 and S. 2213 on constitutional grounds, because both bills would authorize state attorneys general to enforce FTC rules. Enforcing federal regulations clearly constitutes the exercise of "significant authority pursuant to the laws of the United States." Buckley v. Valeo, 424 U.S. 1, 126 (1976). Therefore, under Buckley, if the state attorneys general are to enforce federal regulations they would be "Officers of the United States" and must be appointed in the manner prescribed by Article II, section 2, clause 2 of the Constitution.[1]

In contrast, S. 2326 would strengthen the FTC's own enforcement efforts in this area by authorizing the FTC to appoint state attorneys general to assist Commission attorneys. This approach is superior on two grounds: first, because it avoids the drawbacks of independent state and private enforcement; and second, because it seems likely to increase coordinated efforts of the sort that have proved successful in the past.

In conclusion, the Department of Justice recommends against enactment of the state and private enforcement provisions of S. 2213 and H.R. 4101, but has no objection to the approach taken in S. 2326.

The Office of Management and Budget has advised this Department that there is no objection to the submission of this report from the standpoint of the Administration's program.

Sincerely,

Thomas M. Boyd
Acting Assistant Attorney General

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[1] Article II, section 2, clause 2 of the Constitution provides that the President

> shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the Supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

NACAA // NATIONAL ASSOCIATION OF CONSUMER AGENCY ADMINISTRATORS
1010 VERMONT AVE., N.W., SUITE 514, WASHINGTON, D.C. 20005 (202) 347-7395

September 28, 1988

Mr. Kevin G. Curtin, Senior Counsel
Consumer Subcommittee
Committee on Commerce, Science,
  and Transportation
United States Senate
Room 508, Dirkson Office Building
Washington, D.C. 20510-6125

Dear Mr. Curtin:

Please be advised that the National Association of Consumer Agency Administrators (NACAA) supports H.R. 4101 and S. 2313, regarding telemarketing fraud. It is my understanding that a copy of this letter will be placed in the record of the subcommittee hearing on this matter.

NACAA is primarily composed of the Administrators of federal, state and local consumer protection agencies. NACAA has over 100 members and represents the lead consumer protection agencies in approximately one-half of the states.

NACAA member agencies have grown increasingly concerned with the growing telemarketing problem in the country, its interstate ramifications, and the apparent inability or unwillingness of the Federal Trade Commission to effectively deal with the individual cases. In many instances, those engaged in telemarketing fraud never solicit consumers in the state in which they themselves reside in an attempt to avoid state action against them.

With my own agency, the Georgia Governor's Office of Consumer Affairs, it has been reported to a member of my staff that a Federal Trade Commission staffer was told that she could not investigate an extremely serious telemarketing problem which we turned over to her through my office. Purportedly, this was due to the FTC Enforcement Division's impending settlement with the principle of the company on matters involving one of the principle's former companies. The settlement would have purportedly provided the principle with "immunity" on all of his business dealings up until the date of the settlement. We have been unable to verify whether this is in fact the case, but my office continues to try to resolve problems with the Georgia company, a task made difficult by the fact that, while the company solicits nationwide, it seldom solicits from Georgia consumers, and FTC assistance has not been forthcoming.

This experience with the Federal Trade Commission is similar to that of most of the NACAA member agencies, who have been grossly disappointed with FTC enforcement efforts in this and other areas. For this reason, NACAA most strongly favors the provisions in these Bills which would allow State Attorneys General and other lead state consumer protection agencies to bring actions under the Federal Trade Commission Act. We believe this provision is essential if we are ever going to adequately deter telemarketing fraud in this country.

Additionally, I have a couple of comments upon S. 2326, Senator McCain's Bill on consumer fraud. My understanding is that this Bill would allow the FTC to appoint State Attorneys General to enforce commission rules. I think the public would be better served by replacing this provision with one similar to that in H.R. 4101 and in S. 2313, where the State Attorneys General or other state consumer protection agencies can bring actions to enforce the FTC Act and Rules. Leaving the prerogative as an option for the FTC will likely result in few, if any, appointments with a Federal Trade Commission operating under a philosophy such as the one under which the present commission apparently functions (or does not function).

Also, the State Attorneys General represent approximately only half of the lead state consumer protection agencies; in the other half of the states, consumer protection resides in some other agency. I hope the Committee will keep this important fact in mind, not only on these Bills, but regarding any similar proposals which may come before them in the future. The other states with lead consumer protection agencies other than in the State Attorney General's Office should be included in this provision or some states will be able to enforce, and others, as a practical matter, will not.

Thank you for your attention. Please let me know if I can be of assistance on this or any other matters.

Sincerely,

Barry W. Reid

Barry W. Reid
President, National
Association of Consumer
Agency Administrators

BWR:jhl